

**DISCOURSES ON CONTROL OF CAPITAL EXPENDITURES OF
INDONESIAN LOCAL GOVERNMENTS FROM
FOUCAULDIAN PERSPECTIVE**

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Abstract

This study discusses issues of control mechanisms in the capital expenditure of Indonesian local government, because capital expenditure is the second largest portion of local government spending after the personnel expenditure. Indonesian local governments were chosen as a study sample because Indonesia has been undergoing major bureaucratic reform as a consequence of receiving financial assistance from international institutions. This study involves five local governments from a province, including 64 participants from 37 local government agencies. In addition, this study also uses transcripts of interviews as secondary sources, and makes an extensive examination of regulations concerning capital expenditure.

The findings indicate that capital expenditure involves many parties with their own interests, whereby every party exercises its power over local government for realising a project. Meanwhile, the internal conditions of local governments are still dealing with technical and cultural obstacles to accommodating the interests of all parties. Moreover, local government officials also have vested interests in the use of capital expenditure. Hence, the control mechanisms intended to monitor the capital expenditure of local government are still vulnerable to misuse and irregularities

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List of Abbreviations

Abbreviation	Indonesian	English
APBN	Anggaran Pendapatan dan Belanja Negara	National Budget
APIP	Aparat Pengawasan Intern Pemerintah	Government internal controller
BAPPEDA	Badan Perencanaan Pembangunan Daerah	Regional body for development planning
BKN	Badan Kepegawaian Nasional	National civil servant agency
BPK	Badan Pemeriksa Keuangan	Indonesian government supreme audit
BPKP	Badan Pengawasan Keuangan dan Pembangunan	Indonesian government internal auditor
BULOG	Badan Urusan Logistik	Indonesian bureau of logistics
CGI	-	The Consultative Group on Indonesia
CIDA	-	The Canadian International Development Agency
CSO	-	Civil Society Organisation(s)
CTA	-	Cash Towards Accrual
DAK	Dana Alokasi Khusus	Specific allocated fund
DAU	Dana Alokasi Umum	General allocated fund
DBH	Dana Bagi Hasil	Revenue sharing
DED	-	Detailed Engineering Design
DG	-	Directorate General
DPRD	Dewan Perwakilan Rakyat Daerah	Local parliament
GOI	-	The Government of Indonesia
GTZ	-	German Technical Cooperation Agency
ICW	-	Indonesia Corruption Watch
IDX	-	Indonesia Stock Exchange
IKM	Indeks Kepuasan Masyarakat	Public satisfaction index
IMF	-	International Monetary Fund

IPSAS	-	International Public Sector Accounting Standard
IPW	-	Indonesia Procurement Watch
KEMENPAN	Kementerian Pendayagunaan Aparatur Negara	Ministry of empowerment of government officials and bureaucratic reform
KEPMENDAGRI	Keputusan Menteri Dalam Negeri	Ministerial decree (Ministry of Home Affairs)
KEPPRES	Keputusan Presiden	Presidential decree
KKN	Kolusi, Korupsi, dan Nepotisme	Collusion, corruption, and nepotism
KPA	Kuasa Pengguna Anggaran	Representative of budget user
KPK	Komisi Pemberantasan Korupsi	Commission of corruption eradication
KPPU	Komisi Pengawas Persaingan Usaha	Commission of supervision of business competition
KUA	Kebijakan Umum Anggaran	General policies of budgeting
LKPP	Lembaga Kebijakan Pengadaan Barang/Jasa Pemerintah	Indonesian agency for policies of government procurement
LOI	-	Letter of Intent
MOF	-	Ministry of Finance
MOHA	-	Ministry of Home Affairs
MTI	Masyarakat Transparansi Indonesia	Indonesian community for transparency
MUSRENBANG	Musyawaharah Perencanaan Pembangunan	Development planning forum
NU	Nahdlatul Ulama	The largest NGO with religious (Islam) basis
PA	Pengguna Anggaran	Budget user
PAD	Pendapatan Asli Daerah	Local revenues
PMK	Peraturan Menteri Keuangan	Ministerial decree (Ministry of Finance)
PPA	Prioritas dan Plafon Anggaran	Priority and ceiling of budget
PPAS	Prioritas dan Plafon Anggaran Sementara	Temporary priority and ceiling of budget
PPATK	Pusat Pelaporan dan Analisis Transaksi Keuangan	Center of reports and analysis of financial transaction in Indonesia
PPK	Pejabat Pembuat Komitmen	A government officer who responsible to particular project

PPP	-	Public Private Partnership
PSAP	Pernyataan Standar Akuntansi Pemerintah	Statement of government accounting standard
RENJA	Rencana Kerja	Work plan
RKA	Rencana Kerja dan Anggaran	Work plan and budgeting
RKPD	Rencana Kerja Pemerintah Daerah	Work plan of local government
SAP	Standar Akuntansi Pemerintahan	Government accounting standard
SKPD	Satuan Kerja Pemerintah Daerah	Local government agency
SME	-	Small and Medium Enterprise(s)
TAPD	Tim Anggaran Pemerintah Daerah	Local government's budgeting team
TIPIKOR	Tindak Pidana Korupsi	Criminal acts of corruption
UKP4	Unit Kerja Presiden bidang Pengawasan dan Pengendalian Pembangunan	The president working unit for supervision and management of development
ULP	Unit Layanan Pengadaan	Unit of procurement services
UNDP	-	United Nations Development Programme
USAID	-	United State Agency for International Development
UU	Undang-Undang	Law



Chapter 1

Introduction

1.1. Background of Study

Researchers began investigating designs of organisational structure and accounting control systems during the 1990s. Researchers in organisational theory focus on identifying factors which affect the structure of organisations. Meanwhile, accounting researchers emphasise the nature and extent of accounting-based control, in order to enhance effective planning and decision making (Miah and Mia, 1996). In addition, the wave of ‘new public management’ reforms in the 1980s and 1990s increased the importance of the idea of responsible accounting in the public sector (Modell and Lee, 2001). Furthermore, Modell and Lee (2001) suggested the cornerstone of responsibility accounting is the controllability principle, whereby managers must take responsibility for events and accounting items under their control, which is determined by the organisation structure, particularly in the public sector.

In the 1980s the decentralised organisational structure spread around the developed world. In general, this policy can be viewed from two perspectives: top-down or bottom-up. The top-down perspective perceives decentralisation as a strategy for diversifying responsibilities and crisis management in order to reduce the work overload and financial stress of a central government’s administration. Meanwhile, the bottom-up perspective perceives decentralisation as an expression of self-government. These perspectives are not mutually exclusive and can complement each other (Elander and Montin, 1990). The common rationale for decentralisation is both economic and fiscal, enabling local governments to finance capital investments through long-term debt from the private market. Hence, capital investment enhances the autonomy of local governments and strengthens the fiscal condition of the central government by reducing the grants it distributes. The other rationale is macro-political in that it intends to maintain democratic stability by simultaneously gaining support for its legitimacy and reducing political tension because a regime supported by a small group may cause dissatisfaction and may be avoided by international donors (Guess, 2005).

The governments of Indonesia introduced decentralisation as part of the reformation agenda that was launched in 1999, however, it is regarded as a long term process which aims to make substantial changes and shifts in the behaviour of all governmental actors, i.e. central officials, local governments and citizens. For example,

the process involves a balance between national and local government goals. Hence, the central government needs to regulate the local governments to support national priorities and ensure that they behave accountably and responsibly (Lewis and Smoke, 2008). Unfortunately, the new decentralisation policy has been characterised by the emergence of decentralised corruption committed by local officers. Many heads of cities or districts assume the role of “a king in a small kingdom”, whereby they can determine their own goals without considering the interests of the other cities, districts or the greater interests of the province or nation (Firman, 2009). Moreover, public involvement or pressure from local members of parliament are insufficient to enhance financial accountability and encourage the desired attitude and conduct changes (Harun, 2007).

Despite these challenges, the GOI has devolved a large amount of money, particularly in capital expenditures, to stimulate economic growth in all regions. Local governments allocate approximately 17% of their budget for capital expenditure (Lewis and Smoke, 2008). From 2005 to 2009 government expenditure on infrastructure increase significantly. In 2005, the total expenditure was approximately IDR 20tn (roughly equal to USD2,345,879,950¹), and it increased to approximately IDR 60tn (equal to USD3,060,000,000²) in 2009. The highest increase in capital expenditure for infrastructure occurred in 2008, from about IDR 40tn in 2007 to roughly IDR 55tn in 2008 (Bappenas, 2011). However, a survey on vulnerability to extortion suggests that the situation is influenced by the industrial sector and firm size. This suggests that, in Indonesia, construction and public works companies are the most vulnerable compared to the other sectors (Arvis and Berenbeim, 2003).

Furthermore, capital expenditure in Indonesia is extensive on the central and local government levels. Appendix 1 provides details of capital expenditure on the municipal level from 2006 to 2010, based on data from the Central Bureau of Statistics (*Badan Pusat Statistik / BPS*), and sourced via the official website www.bps.go.id. It covers two types of expenditures, i.e. direct and indirect. Indirect expenditure is allocated to cover governments’ periodic liabilities; while direct expenditure is budgeted based on proposed programmes or specific activities (Darise, 2009). Total expenditure is the sum of indirect expenditure and direct expenditure. Appendix 1 indicates that the proportion of capital expenditure compared to total expenditure ranges from 32.29% to

¹ Assuming exchange rate on 2005 were USD1 = IDR9,830

² Assuming exchange rate on 2009 were USD1 = IDR9,400

21.24%. The proportion of capital expenditure is gradually decreasing every year, in 2006 it was 32.29%, and in the following years it was 30.84%, 28.39%, 25.84, and 21.24% respectively. Between 2006 and 2010 it decreased by a total of 11.05%. The decrease of capital expenditure is followed by an increase in indirect expenditure, which means that the municipal government is still emphasising routine spending rather than capital expenditure because managing indirect/routine expenditure is much easier and more predictable than capital expenditure. The municipal level tends to focus on indirect expenditure in order to meet its budget target instead of direct or capital expenditure.

Appendix 2 presents the ratios of capital expenditure to total expenditure on the provincial level from 2005 to 2010. The table indicates that the ratio is relatively stable compared to the ratio on the municipal level. The ratio for provincial outgoings is in the range of 21.33% to 28.04%. The indirect expenditure at the provincial level is also stable; indicating that the focus of the provincial level is on routine spending and capital expenditure. In addition, examining the ratio of capital expenditure to total expenditure for the central government indicates that the ratio is lower than the ratio for municipal governments or provincial governments. The ratio for the central government is between 10.50% and 15.52%, as shown in appendix 3. These conditions indicate that many capital expenditure projects have been devolved to the lower level, both provincial and municipal, in line with the decentralisation policy.

Overall, the ratio of capital expenditure to total expenditure indicates that the ratio for the local government (municipal and provincial governments) is higher than the ratio for the central government. Hence, capital expenditure on the local level needs to be monitored and controlled properly, because ineffective or incompetent control affects the outcomes and achievements in every area of public policy (Thompson and Jones, 1986). Therefore, this study focuses on the local government rather than the central government. Subsequently, this study explores the perceptions of local government officials, especially relating to the establishment of capital expenditure control in the local government. The reformation of the capital expenditure control system, especially at the local government level, began at the behest of Indonesia's government in 1998 through the involvement of several international institutions. These institutions provided the GOI with funds and stipulate the values to be adopted by all levels of the Indonesian government following the Asian crisis in 1997.

1.2. Local Government Administration

As the institution overseeing the local government, the central government needs to ensure the accountability of the usage of the local governments' resources by requiring local governments to comply with and employ the established control systems (Lewis and Smoke, 2008). This is particularly necessary in the decentralisation era, in which vast amounts of money are devolved to local governments in order to undertake various projects; hence, an efficient allocation of funds requires cooperation between the central government and local governments, in order to achieve national objectives (Aquina and Bekke, 1993). In this context, control is often interpreted as an administrative process designed to regulate the activities of organisations through formal and informal mechanisms such as authority structures, rules, policies, standard operating procedures, budgets, reward and incentive systems, shared values, and information sharing among organisation members (Kenis, 2006; Harrison and McKinnon, 2007). However, these control systems are perceived as inadequate due to their poorly designed mechanisms, weak control and limited oversight by parliament and civil society (Martinez-Vazquez et al., 2007; Mimba et al., 2007).

Historically, finance and accounting systems at the Indonesian local government level have been developed along with improvements in governmental structure. Single entry bookkeeping with a cash basis was employed from 1945 until 1998. Although in some stages it was refined through regulations and laws, the alterations did not change the substance of the system. For example, The regulations (Undang-undang No. 5/1974), laws (Peraturan Pemerintah No. 5 and 6/1976), and *Manual Administrasi Keuangan Daerah – MAKUDA* (Manual of Financial Administration of Regions) of 1981 asserted the implementation of the cash basis and single entry system (Priyono, 2012). Based on these systems, the government could not produce a balance sheet that explained the position of the assets and liabilities of each local government; hence, the local government could not value their own assets and liabilities.

Therefore, when the “New Order” regime collapsed, the people demanded greater accountability and transparency from the government. The government issues regulations regarding accountability to establish a committee to develop and set government accounting standards, which would incorporate an accrual basis and double entry system. Although the accrual basis has yet to be fully implemented, the government has been employing cash towards accrual as a bridging system into full

accrual which is supposed to be implemented by every local government by 2015. Hereafter, all public expenditure by local governments must comply with the requirements of the relevant legal acts and must be recorded, based on the “*Standard Akuntansi Pemerintahan*” (Government Accounting Standards) that are imposed by the central government, in order to enable errors and fraud in public finance management to be identified (Mackevičius and Pranckevičiūtė, 2007).

Regarding transparency, the central government had attempted to strengthen the position of *Badan Pemeriksa Keuangan/BPK* as Indonesia’s supreme auditor, in addition to the *Badan Pengawasan Keuangan dan Pembangunan/BPKP* as the internal auditor of the central government, because their roles were not clear in the previous era. The BPK and BPKP require the publication of audit reports, or at least that the reports are made publically available upon requests. Through these policies, the government has built infrastructures enhancing accountability and transparency. However, administering such a massive nation is not an easy task and Indonesia still suffers from poor governance when compared to other countries in Asia (Scott, 1999; Shankar and Shah, 2001; McGee, 2008; Kamal and Rahim, 2008). The development of Indonesia’s local government and its financial and accounting systems is presented in detail in appendix 4, which is summarised in Table 1.1, and depicts the changes applied to several elements of the old regime by the new one.

Table 1.1 Shifting of several aspects in the old regime and the new regime.

CHANGES	OLD REGIME	NEW REGIME
Organisational structure	Centralised.	Decentralised.
Financial management	Central government managed most of the development funds.	Central government devolves development funding to the local government for management.
Personnel	Central government managed all government officials.	The central government transferred most of the government officials to the local government.
Formal control mechanisms	The central government lacked formal control and the role of government auditors was undermined.	The central government has adopted many best practices, implemented software applications, and emplaced government auditors.

Informal control mechanisms	The central government controlled every aspect of society; particularly the dissemination of information.	The central government liberated dissemination of information, and even endorses it.
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As shown by Table 1.1, this study covers several aspects, including organisational structure, financial management, personnel aspects, and formal and informal control mechanisms, which are specifically related to capital expenditure decisions.

1.3. Aims and Objectives

This study is being undertaken in an attempt to acquire a deeper understanding of the interrelationships and interactions of all actors related to capital expenditure at the local government level of Indonesia following the introduction of new values adopted from international institution by the central government. Hence, in the first stage, this research identifies the actors and how the actors affect capital expenditure decisions. Subsequently, it explores the interrelationships and interactions among the actors, and how the local government officials perceive the roles of those actors in relation to strengthening capital expenditure control. Finally, this study explores how those parties directly and indirectly affect capital expenditure control. This study will identify weak points in the control mechanism by investigating the aforementioned factors. Hence, the findings can be used to strengthen the control mechanism in the future.

In order to explore the dynamics of local government, the researcher employed a case study in a province with a long history of governance as a kingdom, which has abundant references regarding governance practices in this realm. Knowledge of the contents of these volumes is required to comprehend the local values of this particular government that might affect the implementation of the newly introduced values. Hence, the case study approach is compatible with this objective. As this study focuses on the nature of decision-making processes in a particular local government; the findings are unlikely to be generalizable to the other regions which may raise questions regarding its validity. Therefore, in order to enhance the validity of the information collected by the interviews, the data is confirmed by other data from secondary sources, both in the form of interview transcripts and government documents such as laws and regulations.

1.4. Contributions of Study

This study investigates Indonesian local government differently from previous studies. First, none of the previous studies investigated the impact of the vast changes to the financial and accounting systems on local government institutions. This study focuses on the processes of establishing social structure in the organisation of Indonesia's local government, which has barely been investigated (Djamhuri, 2009) and is often neglected because the human resource factor is regarded as statistically insignificant (Mustafa et al., 2011).

Second, previous studies examining capital expenditure of the Indonesian local government focused on quantitative research methods rather than the qualitative approach. The context of this study is capital expenditure in local government, and several studies related to capital expenditure have quantitatively examined how the capital expenditure budget is affected by local revenues (*Pendapatan Asli Daerah*), specifically allocated funds (*Dana Alokasi Khusus*), generally allocated funds (*Dana Alokasi Umum*), and revenue sharing (*Dana Bagi Hasil*), such as (Jaya and Dwirandra, 2014; Wandira, 2013; Nuarisa, 2013; Arwati and Hadiati, 2013).

Third, none of the previous studies investigates control mechanisms from many aspects with emphasising specifically on capital expenditure, either in Indonesia local government or local government of any other countries. Most of the studies on financial control of local government focus on public expenditure in general, such as studies on Comunitat Valenciana – Spain (Balaguer-Coll et al., 2007); Portuguese municipalities (Afonso and Fernandes, 2008); Belgian local government (Borger and Kerstens, 1996) as the sample of their study. While, several example studies with Indonesian local government as the sample are Abdullah & Asmara (2006), Mimba et al. (2007), Djamhuri (2009) and Harun & Kamase (2012). Therefore, this study is expected to contribute to the study on capital expenditure control of local government. In particular, to give an understanding of the rationales of discrepancies between capital expenditure controls that strategically has been established by the central government and the implementation of controls on the local government level.

For current practice, this study is expected to give insights into the social structure in a local government organisation, which should be useful for the central government when introducing new laws or regulations. Hence, the central government can select the appropriate approach to minimise the emergence of resistance from local governments. For instance, in 2008, the central government passed regulation

No.60/2008 concerning *Sistem Pengendalian Intern Pemerintah* (Governmental Internal Control Systems). At present, this regulation is still in the dissemination stage and has not been fully implemented. Therefore, the central government needs to formulate a specific approach to introducing it, by considering the current values of its local governments, in order to achieve an effective standard and level of control.

This study utilises a Foucauldian lens to analyse the interrelationships and interactions among the actors related to capital expenditure. The analysis identifies the types of interrelationships and interactions; in particular, how the actors exercise their power over each other. Many factors affecting the process and mechanisms employed by those actors can be identified in this study. Interviewing primary sources provides much information about the issue of interest, which is supported by secondary sources. Theoretically, this method offers a dynamic framework of local government functioning regarding capital expenditure that distinguishes this study from previous studies on Indonesian local government.

1.5. Organisation of the Thesis

This study is organised into eight chapters. The first chapter is the introduction. It discusses the study's scope and background, the reasons for it, and indicates its theoretical and practical aims, objectives and contributions.

Chapter two describes the nature of Indonesian local government, and the reformation that the GOI is undergoing. It also discusses the role of international institutions' efforts to infuse new values into the GOI. The aim of this chapter is to provide understanding of the values that have been imposed by the central government upon the local governments. In addition, this chapter underlines the existing studies on the financial management of local governments, particularly capital expenditure, and identifies research gaps from previous studies that are filled by this study.

Then, chapter three discusses control mechanisms and Foucault's perspective is employed in this study, which is followed by the development of a theoretical framework. Furthermore, this chapter gives an overview of research methods; discussing the advantages and limitations of the employed method. It also discusses the selection of primary sources in the particular local government, methods of data collection, and the use of transcripts as a source of secondary data.

Chapter four and five discuss the empirical findings from the viewpoint local government officials towards the external and internal parties of the local government respectively. The chapter four focuses on the interrelations of external parties of the local government and identifies actors of the external parties who affect the local government. This discussion revisits several related regulations concerning particular external parties. Then, it is followed by discussing the perception of the local government officials towards the parties in terms of their commitment to strengthening control of capital expenditure.

Chapter five emphasises the dynamics in the sampled local government concerning the implementation of the new values that are represented by new regulations related to the newly prescribed decentralised control system. The aim of this chapter is to comprehend current practices and new values in terms of interrelationships and interactions between the many actors in relation to capital expenditure control. This study relies on interview transcripts from the primary sources.

Chapter six discusses the main empirical findings from the external and internal parties and is followed by a critical analysis and reflection of the findings in relation to their practical and theoretical value in Chapter seven. The final chapter covers the conclusion; a summing-up of the findings of this study, followed by a presentation of the study's limitations and suggestions for future research.

Chapter 2

Bureaucratic Reform in Indonesia Local Government as an Attempt to Enhance Transparency and Accountability

2.1. Introduction

The previous chapter set out the background, scope, and aims of this study, which focuses on issues in capital expenditure control used by the Indonesian local government. This chapter is now intended to give an overview of the nature of Indonesian local government in which the control mechanisms of capital expenditure are employed, along with reforms that have been undertaken by the GOI in order to enhance the transparency and accountability of local government. This chapter also describes the involvement of the International Monetary Fund (IMF), which intensified after the Government of Indonesia (GoI) signed a Letter of Intent (LoI) on 31 October 1997. Initially, the LoI was a survival programme outlined by the IMF, to be implemented when the GoI suffered severely from the Asian financial crisis; and later it was followed up by several further LoIs as a continuation of the programme. The LoI has many facets, such as exchange rates, banking reforms, judiciary reforms, and governance reforms.

The governance reforms embrace reformation of government, empowerment of the private sector, and reformation of civil society. Reformation of the government sector focuses on reinstating the position of the supreme audit agency (BPK / *Badan Pemeriksa Keuangan*), modernising the management of public expenditure and procurement, managing and auditing off-budget accounts, establishing the Anti-Corruption Committee (KPK / *Komisi Pemberantasan Korupsi*), increasing civil service salaries and achieving decentralisation. The decentralisation agenda includes fiscal transfer, civil servant transfer, implementation of accounting standards, and control over financing and expenditure. The reformation agenda relating to the private sector encompasses encouraging a more competitive environment, supporting small and medium enterprises, and endorsing involvement of the private sector in infrastructure projects. Finally, the reformation agenda concerning civil society supports the involvement of members of local society in monitoring local government programmes.

2.2. Nature of Indonesian Local Government

Indonesia is the largest archipelagic state in the world. It is administered by 530 local governments consisting of 497 municipalities and 33 provinces (Depdagri, 2010) spread across 17,508 islands (Indonesia, 2012). In addition, on 25 October 2012

the Indonesian parliament approved the 34th province, meaning that Indonesia now has 34 provinces, which are diverse in many aspects, such as in ethnicity, language, and cultural background.

Structurally, the GOI can be divided into four levels. Level 1 is the provinces, each of which is headed by a governor, who also has a role as representative of central government. Consequently, the governor is answerable to the president. The governor is assisted by a vice governor, and must coordinate every decision with the provincial parliament regarding local ordinance issues. The second level is the municipalities, i.e. cities and districts, which consist of 98 cities and 399 districts. In relation to the second level, the governors have the role of supervising and coordinating the governance of the cities and districts in their province. However, the heads of cities and districts are not responsible to the governor, but directly to central government via the Ministry of Home Affairs. The heads of cities and districts are assisted by a vice-head, and must coordinate with city or district parliaments to approve all local ordinances. The third level is made up of 6694 sub-districts from all over Indonesia. The head of each sub-district is chosen by the head of a city or district to handle certain autonomous programmes in smaller areas. Therefore, they are responsible to those city or district heads. The head of a sub-district is selected from civil servants who are considered to have the capabilities needed for governance. The lowest level is level 4, which comprises 8216 villages. The head of each village is appointed by the head of a city or district, based on recommendations from the head of the sub-district in which the village is located. Hence, the head of a village is responsible to the head of a city or district.

The head of a local government is assisted by a deputy; both officers are elected directly by the people in a particular area or constituency. The head and deputy head of a local government are assisted by a regional secretary as a right-hand 'man', who is selected as a senior civil servant. The regional secretary is responsible for day to day activities, particularly in formulating policies and coordinating with local government agencies, technical units, and sub-districts. Thus, the regional secretary is responsible directly to the head of local government. The local government agencies are vested with autonomy and have tasks to implement and oversee; each agency is led by the head of a service unit that is answerable directly to the head of local government through the regional secretary. Meanwhile, the technical units are formed specifically as support in formulating and implementing the policies of local government. The

heads of technical units are also answerable to the head of local government via the regional secretary.

Following the policy of decentralisation, central government initiated financial decentralisation, which authorised local governments to manage funds, both from central government and from local revenues. For accountability purposes, local governments are required to prepare expenditure budgets in detail, which must be in line with national goals. The budgets are classified based on spending categories, types, and functions, and must then be approved by the local parliament. Expenditure cannot exceed the budget ceiling and cannot be re-allocated to other spending categories unless the revision is approved by the local parliament (Lewis and Smoke, 2008). At the implementation stage, the realisation of the budget may vary; it might lead to under-spending due to the government officials' failure to understand their roles as providers of public infrastructure services. The local government officials continue to perceive that major investments must be carried out by central government. Hence, the focus of the local officers is more on lobbying central government officers in order to make such investments, rather than on planning and managing the investments (Lewis and Oosterman, 2009). Consequently, conditions such as unexpended resources, inefficient spending, and inadequate quality of projects are evident in most local governments (Lewis and Smoke, 2008).

2.3. Reformation in Indonesian Local Government

2.3.1. Factors Influencing the Reformation

Historically, Indonesian politics has experienced turmoil: specifically, in 1998 the military regime that had been ruling for 32 years was obliged to step down (Lewis, 2005). The financial crisis affected Indonesia severely both economically and politically, all of which served to weaken the central government (Green and Campos, 2001), resulting in a change of government similar to the transformation experienced by South Korea and Thailand (Heryanto and Mandal, 2003). With the central government weakened, a separatist sentiment emerged. In order to cope with this situation, in May 1999 the Indonesian Parliament passed Laws 22/1999 and 25/1999 concerning regional autonomy and fiscal decentralisation. The main political reason for implementing this decentralisation policy was to shift the burden and responsibilities of governance from central government to local governments that had ensued after the economic crisis of 1998 (Firman, 2009). It was also expected to bring improvements and efficiency to

government services, because the local governments are closer and more accessible to the people they serve, meaning that they should be more responsive to people's needs and be able to mobilise and coordinate local resources more effectively (Coaffee and Johnston, 2005; Turner et al., 2009; Young and Padovani, 2009; Lewis, 2005). All of those programmes were outlined by many international institutions that came to give assistance to the GOI to accelerate its recovery from the crisis, such as the IMF (the International Monetary Fund) programmes contained in the Letter of Intent from October 31, 1997 up until December 10, 2003.

Following the IMF programmes outlined in the LoI, central government undertook government reform gradually, and determined which institutions need to be reformed. Its first priority was public organisations responsible for state revenues; the second priority was the audit institutions; the third was law enforcement institutions and the judiciary. After that, other ministries or agencies would follow that were regarded as 'less important'. For example, the Ministry of Finance became the first priority, followed by the BPK, the supreme audit board, as the second priority. During the reform processes, these institutions had successfully implemented the concept of a 'balance scorecard' in order to monitor overall strategy, execution of that strategy, and performance of the institutions.

Regarding structural reforms in the BPK, these not only involved the IMF, but also the USAID, which engaged with the BPK in order to improve existing and develop new techniques of investigating, tracking, tracing and recovering assets. Moreover, examinations were to be carried out for the certification of anti-money-laundering specialists. The IMF formally encouraged empowering the BPK in a letter of intent of March 18th, 2003. In this LOI, the IMF suggested improving the accountability and transparency of the government's financial management. In order to achieve these improvements, it was suggested to prioritise finalisation of laws that were in line with international best practices. The proposed laws would complement the previous Law 5/1973, to reinstate the position of the BPK, based on constitutional authority. As a result, the parliament enacted Law 17/2003 regulating state finance, followed by Law 15/2004 regarding the audit of state finance. Then, the GoI issued Law 15/2006 specifically emphasising the importance and position of the BPK.

As a follow-up of Law 15/2004, the BPK required the establishment of generally accepted government accounting standards, standards which, on 17th January

2005, the head of the BPK proposed to the president in order to formulate government accounting standards (Simanjuntak, 2005). The accounting standards did not solely adopt the IPSAS (International Public Sector Accounting Standard), but were also based on best practices and are informed by the government standards of other nations (Islam, 2012). The ‘government accounting standard’ is being implemented gradually, and is aimed at making a transition from cash-based accounting towards the application of a full-accrual method; but currently it is still applying the cash towards accrual method (CTA). However, the implementation of the proposed government accounting standard has had to deal with several issues, both at central government and at local government level, including weaknesses in internal control and the management of financial resources (Islam, 2012), the lack of availability of skilled civil servants to implement the standard (Harun, 2007), and the sub-optimal usefulness of the accounting information for decision making (Mir and Sutiyono, 2013).

With the establishment of a government accounting standard, all of the financial reports have become more rigid, in line with the private sector model (Indonesia, 2003; Harun and Kamase, 2012). Each local government must provide an income statement, balance sheet, cash flow and notes in its financial statement, which is then used as the mechanism that central government uses to oversee the financial performance of local government; this in turn creates and sustains power relations between central and local government. These mechanisms require local government officials to comply with all of the requirements mandated in the governmental accounting standard. Consequently, local government need to upgrade the competency of their officials (Harun and Kamase, 2012), especially financial officials, in order to meet these requirements and get unqualified opinion from the BPK as a supreme audit (Indonesia, 2007).

Apart from establishing the government accounting standard as a basis for reporting, another agenda of the IMF was the reform of budgeting processes, because, in the previous era, the Indonesian administration had been running without a budget. ‘The philosophy at that time was, “Give me the money, and we do the job.” When we entered, it was important to ask, “Why should I give you the money-what job is it?”’ (Salim, 2009), and even ministries or government agencies had off-budget accounts to cover any unexpected expenditures (Green and Campos, 2001). The IMF required financial transparency, and hence off-budget accounts were identified, audited, and brought under a consolidated budget. This task is assigned to the State Audit Board

(BPKP / *Badan Pengawasan Keuangan dan Pembangunan*), which is responsible for internal audits of government institutions. In addition, central government implements budget discipline to rationalise public expenditure, and obliges the bureaucrats to start to prioritise and explain the use of public funds. Following this, the central government budget is presented to parliament for approval. However, the budget consultation process still focuses on lobbying, instead of on conceptual arguments, since parliament is still perceived as underperforming (Tornquist, 2006)

Therefore, in order to cope with any irregularities, the IMF suggested establishing the Anti-Corruption Commission, which was realised by the end of 2003 but only effectively came into operation in 2004. This new body was named the KPK (*Komisi Pemberantasan Korupsi* / Commission of Corruption Eradication) (Schutte, 2012). The institution has responsibility for preventing, investigating, and prosecuting corruption cases. In order to facilitate the carrying-out of these duties, a special court for dealing with corruption cases was established, i.e. Tipikor (*Tindak Pidana Korupsi* / Corruption) court (Jacobs and Wagner, 2007). The court has maintained a 100% conviction rate of corruption cases, and the KPK has prosecuted many prominent politicians, ministers, and governors, as well as officials of the Indonesian central bank. Consequently, some police, prosecutors, and parliament members that were under the scrutiny of the KPK orchestrated a fight back and managed to weaken the KPK and the Tipikor court (Butt, 2011).

The World Bank also played a role in the reformation by working with the Kemenpan (Ministry of Apparatuses Empowerment and Bureaucratic Reform) along with other ministries to bring in people from the private sector, independent experts, and consultancy firms. They held a forum for sharing and learning with many experts from various countries, such as Malaysia, Korea, Singapore, Italy, Germany, Australia and Sweden, in order to accelerate organisational restructuring to make it more efficient and more effective. To this end, employing technology was considered to be a priority at that time in Indonesia's reforms. There were several reasons for this: the first was to minimise personal interactions that could possibly create a temptation to behave corruptly, which would thus enhance good governance. The second reason was the need to build information systems to support human resource administrations, since the current information system was fragmented and negatively affected both the quality and accuracy of data. This meant that the data could not be relied on; for example, there was a lack of data pertinent to the competence and background of staff. Even more

disturbingly, some names were still on the old database, although that person had by then retired or passed away.

In 2000, the Indonesian government held a meeting with the CGI (Consultative Group on Indonesia) that was supported by the World Bank and the CIDA (Canadian International Development Agency) in order to endorse the implementation of the decentralisation process by determined planning and staging. The meeting decided upon the stages of implementation, breaking them down into initiation, instalment, consolidation, and stabilisation; they also decided on relevant targets. The initiation stage was undertaken in 2000; 2001 and 2002 were designated for the instalment period; 2003 and 2004 were for the consolidation period; and finally 2007 was expected to be the stabilisation period. However, the implementation plan did not go as well as expected, due to a lack of effective communication between the central government and local governments. Hence, central government amended Law 22 of 1999 into Law 32 of 2004 that still reflected enthusiasm of decentralisation. Moreover, the law of 1999 was perceived as being motivated more by political than fiscal reasons (Pepinsky et al., 2009).

Another international institution involved in the reformation was GTZ (German Agency for Technical Cooperation), especially in running of 'good governance' programmes. Donor institutions such as GTZ did not impose their programmes, but raised awareness of and gave insight into the reformation of all levels of government. This process also involved bilateral donors such as Australia and New Zealand, which assisted in designing government organisations that would eliminate corruption or financial irregularities practices (Hamilton-Hart, 2001). As a result, the structure of the ministries and agencies in Indonesian public administration has been transformed; it is now more regimented and rigid in order to enhance the performance of the bureaucracy so as to deliver an effective and efficient public service (Datu and Nawawi, 2014). Therefore, selection and placement of the right person in the right place is essential.

2.3.2. Pros and Cons of the Engagement of International Institutions

Since the first time the GoI engaged with the IMF, from 31st October 1997 to 10th December 2003, about 20 Letters of Intent (LoI) have been signed by the GoI concerning many aspects of government reforms in Indonesia. The IMF did not only offer technical assistance for the implementation of the reforms but also provided funds

that were equivalent to SDR 7.3 billion or 490 percent of the quota (IMF, 1997). The GoI at that moment was suffering from a macro-financial problem because the exchange rate had plummeted from USD1 = IDR2,432 in mid-July 1997 to USD1 = IDR11,050 by the end of January 1998 (Habibie, 2006). Consequently, overseas loans rose to USD140 billion (about 60% of GDP), of which USD33 billion of the loan was short term (IMF, 1997). Hence, this condition aggravated the financial burden the GoI was under. Moreover, internally, 16 banks were shutdown and the GoI had to bail out those major banks that could be salvaged, increasing the financial pressure on the GoI, driving it to the IMF to get the funding to meet the nation's obligations.

The IMF then set up a three year stand-by funding arrangement (IMF, 1997) which came from many sources such as the IMF, the World Bank, the Asian Development Bank, Japan, Singapore, the US, and four other Asian countries (Head, 1998). According to Soesastro (2009):

They were very reluctant at the beginning to do so, the Fund, the International Monetary Fund, saying that this is not the area of our competence. We know nothing about structural reforms, reform of the manufacturing sector, trade and so on, it is only the financial sector that we wanted to include in the package, including fiscal and so on, but not structural policies. It was the World Bank that said you have to. The Indonesian ministers also said we have to put it in. In fact, even outsiders like us said it is important.

The GoI was provided with emergency procedures that would be reviewed quarterly in the first-year programmes. Under these conditions, the GoI was obliged to follow the IMF lead regarding macroeconomic policies and financial sector restructuring. The GoI was required to adhere to any decisions that it was decided must be taken by the IMF to resolve the multi-dimensional problems facing them. This situation gave excessive power to the IMF, which acted as a governing actor and dictated any policies that should be taken by the GoI. After this, the IMF started to implement systems through many policies, referring to the best practices that were perceived as the best way to resolve Indonesia's problems.

The IMF set indicative measures, along with target dates, to be met, and determined what action or actions had to be taken. If the GoI could not meet the target, or did not comply with the LoI, the IMF would discontinue the funding. For example, before the GoI signed the LoI on 24th June 1998, the IMF discontinued the funding to assist Indonesia's recovery from the financial crisis. After the GoI stressed its full commitment, as expressed by the president in his speech on 21st May, 1998, the IMF

once more began to channel their funding. By the end of July, the consortium known as the IGGI (Inter-Governmental Group on Indonesia) increased loans to Indonesia, and the “Paris club” (an association of countries providing loans to Indonesia) decided to postpone repayment instalments of Indonesia’s debt, which indicated the growing confidence of lenders in Indonesia (Habibie, 2006).

With the signing of the LoI, the GoI was placed under the control of the IMF, and had no bargaining power regarding the recommended programmes. This situation can be perceived as a new model of colonialism, i.e. a form of economic colonialism in developing countries. This view was expressed by the former Coordinator Minister of Finance and Industries (Kwik Kian Gie), who perceived affiliation between the World Bank, the Asian Development Bank and the IMF as external forces determining the economic and financial policies of Indonesia. These international institutions were the biggest donors supporting the financial recovery in Indonesia when the country was hit by the Asian financial crisis (Head, 1998). They suggested many policies outlined in the LoI which were perceived as being inflicted on the GoI. One such policy was a relaxation of the import duties on rice and sugar, because domestic production for these commodities was abundant. The policy was detrimental to farmers because Indonesia is known as a producer of both rice and sugar. Hence, the domestic price of rice and sugar rapidly declined (Gie, 2011). Moreover, Gie (2011) explains that before 1945, the Dutch exploited Indonesia through the country’s valuable crops and human resources. However, after 1967 these international institutions had exploited mineral resources through the latest methods and technologies. From this perspective, we can see that Indonesia had surrendered its sovereignty to various international institutions and had started to be governed by those international institutions.

Moreover, the IMF assumed that the best practices that had been suggested were suitable for Indonesian society because they could be implemented in various conditions and by different cultures as a one-size-fits-all, global panacea. This was exemplified by the discussion between a former coordinating minister for economic affairs and Dr. Hubert Neiss, Director of IMF Asia, about whether or not to raise the price of fuel during the rising political temperature in Indonesia. A decision which was based only on a superficial observation of the country without considering any of the socio-culture dimensions of Indonesian society:

I said to Neiss, as an economist, I fully understood the reason to increase the oil price, but Indonesian political temperature is high already. If you push this,

something will happen. Dr. Neiss with his cockiness, he doesn't understand Indonesian politics. He is a good economist. He said, 'You are exaggerating. Every morning I use my shorts, my jogging outfit. I jog behind the Grand Hyatt in the poor area of Kebon Kacang and what I see is Indonesian smiling.' (Ramli, 2009)

The consequences were disastrous, as the decision triggered uprisings in many regions and aggravated economic and social conditions as well.

They (the IMF) increased the BBM (*Bahan Bakar Minyak*, oil fuel) gas selling price 71%, something, and the day after that decision there are major demonstrations and the burning of Makassar on May the 2nd. On May the 3rd, Medan was burned, major demonstration and it goes into Surabaya on the 4th, the 5th. Solo was burned. Hundreds of people are being hurt in Jogja (Yogyakarta) and Solo and then it ended May 12th, of 1998 in Jakarta when buildings all over the city were burned. ... Thousands of people were killed and I consider this is a nightmare, IMF-provoked riots, like what they have done a lot in Latin America and Indonesian rupiah dropped IDR15,000. Forty million people laid off, the whole economic consequences of using economic policy for political change, it's huge. The human, the moral cost of it is huge. (Ramli, 2009)

The GoI did not have the power to reject the arrangement, and so implemented the programmes as indicated in the LoI, along with technical assistance from the IMF. This showed that, although the suggestion was feasible economically, it was not feasible socio-culturally.

Another example of an IMF recommendation that caused controversy and opposition was liberalising the economic system in Indonesia, which had previously been situated in the middle between socialism and liberalism. In the prior system, important natural resources and companies were still managed, controlled and monopolised by the government in order to maintain the welfare of society. However, in accordance with the LoI's recommendations, the GoI agreed to privatise several strategic state-owned companies and banks; these were later bought by international companies because most of the Indonesian companies were still struggling to survive the financial crisis. This is indicative of the fact that the IMF neglected the local socio-cultural make-up, which can be seen as a communal rather than an individualistic society.

However, perceptions of the IMF programmes were not shared by all ministers. On one side, a group of ministers and advisors supported the implementation of the programmes, and perceived that such actions would be able to resolve the multi-dimensional crisis. As expressed by one of the secondary sources:

the more important reforms instituted under the IMF packages were institutional reforms, governance basically, good governance. (Soesastro, 2009)

Furthermore, the former Minister of Finance admitted that, even though it was not a good way to undertake reform, having reforms enforced by other, external institutions was like a blessing in disguise:

We could be very, very disappointed because crisis induced reform is not well thought out reform, it is urgent reform, it is advanced by the situation, it is enforced by other institutions like the IMF (International Monetary Fund) program and so on. (Indrawati, 2009)

The later source gave full support for the implementation of the IMF programmes outlined in the LoI and focused on achieving the targets.

Opposing them, a former Coordinating Minister for Finance and Industries resisted the involvement of the IMF; he suspected the involvement of what he called the 'Berkeley Mafia' as cronies of the IMF, the World Bank, and the Asian Development Bank, ensuring their control over Indonesia's economic and financial policies (Gie, 2011). Officially, the GoI was under the control of the IMF until 2003, when the IMF produced its final review, under the extended arrangement, on the 10th of December, 2003.

Resistance to the involvement of the IMF in Indonesia's affairs was not only expressed by the next president after Soeharto, as described by a secondary source as follows:

Abdurrahman Wahid's ministers were all against it. The coordinating minister for the economy in fact sabotaged. Because he came from a political party, PDIP (*Partai Demokrasi Indonesia Perjuangan*), that is totally against the involvement of the IMF. He is the coordinating minister who is in charge of this. When they negotiate a package with the IMF-in fact, he didn't want to participate and said, 'It is totally yours.' So the IMF was very frustrated, and they came to see members of the National Economic Council and said, 'We can't work like this. It has to be your package, not ours.' (Soesastro, 2009)

Nevertheless, resistance occurred from the first time that the GoI engaged with the IMF, when President Soeharto was still in power. He was perceived as very combative, and did not comply with suggestions outlined in the LoI. His position was supported by the Minister of Science and Technology, who later became vice president and then became president, replacing Soeharto when he stepped down. The minister was in charge of all strategic industries (Soesastro, 2009) such as land, sea, and air transportation, machines, and military weapons (Habibie, 2006). The resistance possibly arose because the IMF

suggested closing down the strategic industries without any rational reasons. This was despite one of the industries being able to produce aeroplanes suitable for the geographical conditions present in Indonesia: planes which had been certified suitable to fly. Moreover, the industries had been able to produce military weapons, vessels for sea transportation, and military ships (Habibie, 2006).

This policy can be regarded as an intervention by the IMF to protect the interests of the donor countries, because if Indonesia could not produce all of these products, then the GoI would be dependent on the other countries and buy all their products from them. Therefore, in order to eliminate the intervention of the IMF, the GoI decided to end the IMF programmes, and repaid the entire loan in 2004. Subsequently, the new programmes were introduced and initiated by the GoI itself, superseding the IMF programmes (Soesastro, 2009).

2.3.3. Agenda of Local Government Reform

2.3.3.1. Decentralisation

The main agenda of the LoI of the IMF was devolution of power from central government to local government, and the IMF and the World Bank coordinated with parliament to ratify this agenda. Legislation was arranged carefully to establish a legal basis before proceeding with decentralisation reform and administrative decentralisation, as well as the expenditures and revenues that might be incurred or accrue from the policy respectively. For example expenditure required to set up facilities for the decentralisation processes or revenue acquired by central government through the implementation of the DBH (revenue sharing). The UNDP (United Nations Development Programme) was also involved in promoting decentralisation by embracing its principles, actions and budgetary considerations. For the implementation of the programme, the GoI provided a budget of about IDR1.02 trillion, equal to around USD1 billion at that time, plus IDR94 billion, which was roughly USD94 million from donor countries, channelled through the UNDP.

These conditions stoked up enthusiasm for the creation of new districts or new provinces, but without any consideration being given to the region's developmental potential. Instead, the main idea was to get as much money as possible from central government (Devas, 1997) and give locals the opportunity to become a member of the elite executive or legislative bodies. Once obtained, the funds from central government were then used for administrative spending, such as on government officials' salary and

government offices, rather than investment or infrastructure to generate new opportunities. This conduct reflected the poor governance and lack of accountability at local government level (Sjahrir et al., 2014). In addition, the increase in the number of local governments also enlarged the bureaucracy and increased the number of bureaucrats, which required the recruitment of local people.

Creating new districts or cities increased the number of local governments from approximately 420 in 1998 to a current total of 514. Since decentralisation is directed at the municipal rather than the provincial level, this raises a problem regarding the extent of central government's reach over the municipalities. Therefore, central government delegates its coordination function to its representatives at the provincial level. However, there is no formal, subordinate relationship between the municipalities and the provinces; hence, the municipal administration might well ignore the intervention of a governor, who has no legal power over either the districts or cities in their region / province because the municipalities are structurally responsible to central government rather than to provincial governments. Ideally, if the decentralisation process is managed properly, it creates a conducive environment for democratic development by effectively diffusing administrative power (Rabasa and Chalk, 2001).

Another issue in the creation of a new district arose from local sentiment, and especially the idea that the *putra daerah* (the region's indigenous people) should be leaders of regions (as governors, regents, or mayors). The problem with this idea is that the quality of human resources of the newly autonomous regions was and is still low (Devas, 1997) – problematic because the roles of leaders in governance reform are crucial, especially in providing a model for strengthening economic development in a particular area. Moreover, local leaders must be able to control, manage and lead, which means they must have a firm grasp of regulations, procedures, local ordinances, codes of ethics and codes of conduct in order to ensure tight control, as any violations of any of such legal matters could well mark the beginning of a problem.

This issue becomes especially prominent for regions located in the outer islands because of the unequal economic and human resource development between Java (where the capital city is located) and the outer islands. The mindset of the previous regime was that if the outer islands became well-developed, then the threat of separatism from those islands would be greater than from those which were less-developed. Hence, currently Java has become the centre of the economy, and the

quality of human resources in the outer islands is relatively low in comparison to Java and its surrounding islands. It has even been suggested that 30% of regencies cannot meet the standard of autonomy legislation that has been set by central government, and that the other 70% only meet the minimum level, which negatively affects their transparency and accountability at the local level (Rabasa and Chalk, 2001). Moreover, geographical conditions are regarded as a trigger affecting regional development, which must be taken into consideration as well (Pepinsky et al., 2009).

In the previous era, decentralisation had become a concern of central government, leading to it issuing Law 5/1974, but this regulation could not meet the expectations of the regions as there was no derivation from the regulation to support the implementation of the law. When a moment for decentralisation emerged in 1998, central government facilitated the demand by devolving more resources and power in order to eliminate separatism movements, which had been flaring up in several regions (Rabasa and Chalk, 2001). This decentralisation was, and is still, intended to strengthen Indonesia in general by giving more autonomy to local government, as well as embracing local culture, supporting economic distribution and facilitating political expression by devolving power to local regions.

The basic idea is that if decentralisation manages to enhance economic performance at the local level, then it should improve the national economy as a whole (Pepinsky et al., 2009). However, decentralisation is regarded as too far-reaching by one of secondary sources (Nurbaya, 2010), as the power is devolved to districts and cities rather than just to the provinces. Initially, the President considered that if power were devolved only to the provinces, provinces would then still have the power to demand independence from central government; but if devolution were extended beyond them, to the lower levels of districts and cities, any intention to separate from central government could be eliminated, as the municipal regions are too small.

In May 1999, the government issued Law No. 22 regarding regional development, which it intended to be implemented within two years after it was issued. In order to accelerate the implementation, the government divided the MoHA into two ministries, i.e. the MoHA and the Ministry of Regional Autonomy. From this point onwards, the regions would take their entire problems to, and consult with, these ministries, and therefore the engagement of the regions with these ministries was intense when compared with the other ministries. However, coordination between the

two ministries did not go well, especially in matters related to law-making and regulation processes, following changes in administration, which then had a significant impact on other aspects of governance. These regulations were thus perceived as being unable to fully accommodate the reformation processes. Each ministry pursued its own agenda, and, as a consequence, implementation of Law 22 was slow, due to the absence of technical guidance and a lack of knowledge of the details comprising the regulations. Therefore, there was criticism that the decentralisation policy lacked adequate structural planning to support the implementation of the policy (Rabasa and Chalk, 2001). Finally, in August 2001, the Ministry of Regional Autonomy was reintegrated into the MoHA.

In these decentralisation processes, the MoHA also dealt with the transfer of assets and government officials from central government to local governments. In addition, a new law, No. 32, marked out clearly which areas were to be managed by central government and which areas would be managed by local government. This law determines six areas controlled by central government: i.e. national monetary and fiscal affairs; foreign affairs; religion; national security; defence; and the judiciary. Referring to this regulation, central government determines the assets, personnel, and administrative tasks to be devolved to local government. Thus, following Law 32, not all issues are decided in Jakarta. This makes decision-making much easier, because of the geographical constraints in Indonesia (Klinken, 2013).

2.3.3.2. Fiscal Transfer

While the transfer of assets and government officials from central government to local government were handled by the MoHA, the Ministry of Finance implementing the fiscal transfer. In the first step, the ministry changed the fiscal year, which previously ran from April to March, to January to December. The new fiscal year arrangement began on 1st January 2001, which marked the start of the instigation of Indonesia's regional autonomy. The Ministry of Finance also initiated laws regarding fiscal balance, which require central government to collect all revenues and then distribute the funds to all regions in an attempt to ensure equitable distribution among regions. The grant from central government that encompasses DAU, DAK, and DBH thus significantly affects local government development (Kappeler et al., 2013).

In the previous era, highly centralised governance resulted in a fiscal imbalance between central and local government, as central government collected 90% of the

revenues, and only 10% was collected by local authorities. Decentralisation has played its role in reducing the government's and nation's fiscal imbalance, but on the other hand, it can also be seen to have increased the gap between poor and rich regions (Rabasa and Chalk, 2001). In order to reduce the gap, central government allocates funds through many channels for specific purposes. The main allocations are via the DAU, DAK, DBH, *Dana Penyesuaian*, and *Dana Otonomi Khusus*. However, it is suggested that, on average, only 30% of the total budget benefits the public domain, since about 70% of the funds are allocated to bureaucrats, political parties, and parliament. Proportions of fund allocation from central government from 2012 to 2014 are presented in appendix 5.

Initially, the percentage of distribution that was received by the revenue-producing regions was determined by negotiation with central government, and it was determined that those regions must be well informed with regard to the calculation of the percentage. It should be pointed out that this system was highly affected by political conditions and considerations, and, in order to deal with these phenomena, laws concerning local revenues and fiscal balances were revised several times, i.e. in 1999, 2004, and 2010. Subsequently, the Ministry of Finance also dealt with finance transfers from central to local government, developing a new format for the implementation of such transfers.

The first allocation is the DAU (*Dana Alokasi Umum* / generally allocated fund), coming from the national budget and intended for equitable distribution of income among the regions. This fund is used to finance regional needs as a component of the implementation of the decentralisation programme (Indonesia, 2004). Central government does not merely employ population numbers as a criterion for allocating funds, unlike the previous era, which focused its development drive on Java, which received the largest allocation as the most populated island in Indonesia; instead, the government emphasises under developed regions, especially the outer Java islands. Basically, central government has developed a matrix with four quadrants which consists of low-growth – low-income; low-growth – high-income; high-growth – low-income; and high-growth – high-income. Rich regions included in the low-growth – high-income quadrant need to be pushed to undertake policy reforms in order to shift them to the high-growth – high-income quadrant. Equally, if there are some regions in the low-income – low-growth quadrant, this means that central government needs to pay more attention and allocate more money to the regions.

The second source of local government funding is the DAK (*Dana Alokasi Khusus* / specifically allocated fund), which is allocated from the national budget to particular local governments to finance either specific central government programmes relating to a particular local government, or specific local government programmes which conform to national priorities (Indonesia, 2004). This fund is intended for specific needs that cannot be predicted in general terms and gets its funds from the DAU / generally allocated fund. Specifically, it is allocated mostly for infrastructure development with a long economic life, and the individual local government must also participate in these processes, i.e. the 10% of the total DAK that has been given by central government. For example, if the central government grant for DAK is worth USD100,000, then the local government must provide USD10,000 in addition to the central government's grant (Badan Pemeriksa Keuangan, 2011).

The other source is DBH (*Dana Bagi Hasil* / shared revenue fund), which deals with the revenues from central government apportioned to regions based on the potential of those regions. This fund is acquired from sharing the revenues derived from taxes and the exploitation of natural resources. The sharing mechanisms are based on the 'origin principle' and realisation of revenues. Previously, rich regions contributed revenues from forestry, minerals, gas and oil, but they received the least money because most of the funds were managed by central government. Therefore, central government tries to balance this situation, and as a result local regions currently receive revenue proportionally. However, this arrangement also creates environmental issues in local regions. For example, a correlation between decentralisation and deforestation has been indicated, because there is no guideline regarding the ratio of green to non-green areas. Hence, the rate of deforestation is identical with that of decentralisation, because the majority of local government administrators are elected with support from local business; hence, in return, those businesses are given timber concessions.

2.3.3.3. Civil Servant Transfer

Regarding personnel transfer, the MoHA collaborated with Kemenpan (*Kementerian Pendayagunaan Aparatur Negara* / the Ministry of Empowerment of State Apparatus, later known as the Ministry of Empowerment of State Apparatus and Bureaucratic Reform) to transfer government officials away from central government in order to strengthen the institutional capacity of local governments (Bennet, 2010). In

the previous era, all government officials were managed by central government, and at that time central government controlled more than 2.1 million civil servants. The decentralisation policy aimed to transfer many of these civil servants out by the end of 2001. The transfer was expected to reduce the numbers on the central government payroll by 1.6 million. But this process of personnel-transfer provoked unrest among the government officials because they were central government officials but would be transferred under the management of local government, a novel arrangement which was unknown in terms of the sustainability of local government. However, the transition process was accomplished relatively smoothly, although at the beginning local governments still employed the old organisational structure.

2.4. Impacts of Reformation in Multidimensional Aspects

2.4.1. Impact on Government Officials

Bureaucratic, civil service and political reforms were undertaken at the same time, but civil service reform was perceived to lag behind the other two. Some important positions were still held by people who lacked competence in a particular field. Such individuals were in position based on their seniority instead of performance levels; a carry-over from the previous era, when loyalty was more important than efficiency. Therefore, improvements in the competency and capability of the civil servants rely upon the policies and rules from the Kemenpan that the line ministries must comply with. However, the Kemenpan has been struggling to improve its own internal human resources, due to its important role as Indonesia's think tank for advancing methodologies or mechanisms for civil servants that will be referred to by the other ministries, specifically for laws related to civil servants. For example, if the Ministry of Finance would like to implement performance management, it must consult with and get approval for such an initiative from the Kemenpan as the central authority for competence and the BKN (*Badan Kepegawaian Nasional* / National Civil Service Agency).

It has been predicted that, of the staff inherited from the previous era, 30%-40% are unproductive, but they receive the same amount of salary. This condition demotivates the productive staff, as they feel they are being treated unfairly, relative to their unproductive colleagues. Therefore, an assessment centre and mechanisms to measure the competency of staff has been created, along with a training system to ensure that personnel are trained up to understand and deal with the new systems and

procedures. Personnel are expected to deliver a high standard of performance, but they are rewarded with fair and reasonable salaries proportionate to their workload and responsibilities (Setiyono and McLeod, 2010). Therefore, ministries have also set up new incentive schemes based on the performance of their staff. Hence, if a staff member delivers a good performance, then he/she will get a higher incentive bonus and remuneration. Although they are now paid with a higher salary, some civil servants can still be found who underperform in their workplace. Rewarding staff by increasing their salary and benefits is perceived as not positively affecting these staff members' behaviour, as the officials might well be receiving bribes of greater value from outside. Doing something about this type of civil servant, particularly in a highly corrupt government system, is still regarded as an extremely difficult task (Hamilton-Hart, 2001; Setiyono and McLeod, 2010).

In order to deal with this issue, governance reform has begun to implement the balancing of rewards and punishments. The punishments encompass either psychological or material aspects. Psychological punishment can be a demotion of staff from their current position; this kind of punishment is regarded as harming the individual's pride, and hence the punishment is perceived to be more effective when applied to a staff holding a higher position than to a lower-level staff. Meanwhile, for a corrupt civil servant, a material punishment needs to be implemented, with a requirement for them to return the stolen funds. In addition, the staff will be convicted as a criminal and will be given administrative sanctions as well.

Nevertheless, honest, ethical behaviour all depends on the power and capacity of the leader to displace officials who do not comply with the reform programmes. In order to make such a system effective, open commitment of the leaders to governance reform needs to be initiated by the president and all ministers, parliament members and local government leaders, and all judicial branches. The commitment must be embodied by giving positive examples, such as not practising cronyism, and by respecting laws, bureaucracy and meritocracy, because in Indonesian culture good, clear examples can make the concept of reform easier to understand. Moreover, consistency is also needed in structuring, closely monitoring, evaluating and restructuring the governance system, all of which demonstrate the leader's concern with reform.

Therefore, strong leadership is needed in government organisations, and sometimes an 'overkill' punishment is necessary in order to send a powerful message to

all members of a ministry or department. For example, take the case of the Bulog (*Badan Urusan Logistik* / The nation's state logistics agency). In the previous era, it was common to bribe the top-level officials of the Bulog to secure a placement of a government official in a rich area, which had huge amounts of money in circulation. However, when the new leader came up, he rotated 200 officials from the 'rich' areas to the 'poor' and outer areas in order to send his message that he did not want any bribery within the system. However, the capacity of leaders or ministers to exert control in public organisations is extremely sensitive to and highly affected by political change. After the general election, every 5 years, most ministers will be replaced by new ministers; it is quite possible that the new minister will promote people from his or her affiliated political party without any clear indicator as to the degree of the appointee's talent. As a consequence, this practice might well demoralise other, talented civil servants within that ministry or agency.

2.4.2. Impact on Organisational Culture

Many leaders of government institutions lack an understanding of what the reform is because the reform is perceived as offering increasing remuneration and solely focusing on regulations and policies; it is thus regarded as being an inherently incomplete reform. The reformation suggested by Ministry of Finance official needs to start by overhauling business processes for improving public services that are expected to regain the public's trust. For example, reformation of the Ministry of Finance began with reviewing the standard operating procedures and then simplifying the business processes by automating some areas by combining IT with certain procedures. These steps were followed by reviewing job descriptions, analysing jobs and workload, building an assessment centre that would affect any additional bonuses, setting up a human resource information system, and then enhancing the quality of human resources by recruiting new staff from the pool of high-quality new graduates.

The governance reforms at this moment are relatively complex, as they not only focus on hard-control related to procedures, laws and regulations, but also to soft-control emphasising socio-cultural aspects currently encountered in government: for example, ineffective infrastructure development and government spending are induced and facilitated by counterproductive bureaucracies either in central and/or local government. Therefore, in order to change the cultures of internal organisations, the leader must have the courage to challenge officials in structural positions who hold

established positions and who are regarded as ruling little kingdoms in a particular ministry or department. However, this approach is not supported by existing regulation, and it is not easy to discharge a government official unless he is caught red-handed committing a serious crime, or is in grave violation of civil service regulations.

In addition, concerning the organisational culture of government organisations, it is necessary to establish an egalitarianism climate in which an individual can speak up if something wrong occurs, and where any ensuing judgements are not be based on ethnic or religious affinities. This bureaucratic mentality is still dominant among government officials, inherited from the previous era where the working environment tended to impede the critical and creative thinking of officials (Harun and Kamase, 2012). Moreover, socio-cultural structures in Indonesian government institutions are very strong, an *esprit de corps*, meaning that it is considered inappropriate to shame a member of the group, and hence attitudes are very permissive towards underperforming staff or even those violating the rules (Irawanto et al., 2012). Hence, it is now a preferable option to recruit new personnel, rather than attempt to re-educate the old staff; young, talented workers can be shaped easily, and are perceived to be able to change socio-cultural attitudes and values in public organisations, enabling them to become more open-minded. They have the courage to argue with their superiors, which rarely occurred in the previous era.

Another issue relating to governance reform is interaction among departments or ministries, as expressed in a secondary source from a senior economist:

There was rivalry between departments. You see, the departments used to have money, and they are the kings in their own sectors. Therefore, it needs inter-sectoral (across departmental) coordination and cooperation. The government officials do not really belong to the government; you belong to one department, a department which demands your loyalty: the department symbols, the department songs, the department association. I mentioned with so many departments, (it is) ego-sectoral. How can you build one civil service? That was a big battle. ... The whole system of government was very much ego-sectoral. (Salim, 2009)

Hence, it is not easy to draw personnel from other departments, as the current system encourages departmental loyalty rather than a wider inter-departmental perspective. In order to deal with this issue, the ministries or agencies are compelled to formulate an integrated system. At the national level, there is the National Reform Team, which consists of the Kemenpan (the Ministry of Apparatuses Empowerment and Bureaucratic Reform), the Ministry of Finance, and the KPK (Commission of Corruption Eradication), which make up a coordinating forum to discuss policies and regulations

across institutions in a more structured way; this forum can also revisit policies that have been implemented.

However, this kind of forum is susceptible to political dynamics, because the current political system encourages domination by national elites (Faguet, 2013). When many political parties are involved and hold power in many departments, then conflicts of interest will be prominent, rather than when the organisation is managed by a professional appointed by the President. This condition is due to the composition of ministries in the Indonesian government, as approximately 61% of ministers are from political parties (Echwan, 2009). The historical roots of each political party affect the behaviour of each political actor differently (Peters, 1999; Blau, 1970; Barley and Tolbert, 1997) because each party has own values that affect the activities and relationships within the organisation (Barley and Tolbert, 1997). When a political actor has a position in a ministry, the values of his/her party affect them significantly. As Eisenstadt (1964) indicates, parties will tend to fight for their own interests within the existing systems, and use the systems as vehicles for their political benefit (Dix, 1992). In line with this, Eisenstadt (1964) suggests the need for the creation and institutionalisation of norms of social behaviour, along with sanctions, all of which will regulate the behaviour of an organisation's members who come from different cultures or political ideologies (Eisenstadt, 1964).

Lack of coordination does not only occur between ministries, but also between ministries and local governments, leading to public funds being spent without considering the benefit for the local government (Mello, 2000). As formal organisations, ministries and local governments must have a system to coordinate and control activities (Meyer and Rowan, 1977; DiMaggio and Powell, 1983). Local government is required to conform to the regulations and policies that have been established by central government (Meulen, 1998). However, in many cases, local governments reluctantly adopt the prescribed systems, which might not fit with their needs because every local government has its own different characteristics (Meyer and Rowan, 1977). As a result, interrelationships among ministries, local government and local government agencies may seem to be attached, but in some aspects they remain circumscribed, separate and slow to respond (Weick, 1976).

2.4.3. Impact on Engagement of Private Sector

Apart from governance reform, the private sector has also been put on the IMF agenda to be empowered. The basic idea is that in the market mechanism/model, when a buyer buys for himself and the sellers sell their own product or service, then there is no opportunity for corruption. However, when government officials, who hold authority over resources, get involved in these business activities, opportunities for corruption do emerge, because corruption can occur when one party has control over resources, but does not own them. Since corruption is inefficient and raises costs, this will put a company at a competitive disadvantage in the market paradigm (Hipsher, 2013).

Therefore, interaction between government officials and the private sector is encouraged to be more transparent, as the private sector is suspected of engaging in mark-up or bribing government officials in order to secure government projects through procurement mechanism. The idea of transparent interaction has been imposed by the KPK (Commission of Corruption Eradication), as currently the KPK does not only prosecute politicians and public sector officials who receive bribes, but also companies and individuals in the private sector which offer bribes. Everyone who takes part in the activity will be charged. The KPK's actions are intended to make people worry about bribing government officials to enhance their business interests. Therefore, the dissemination of information, guidelines and legal interpretations is required in order to eliminate any legal uncertainties concerning the acceptable behaviour of government officers and others (Magiera, 2011). In addition, government officials need to understand the nature of the business world, which needs businesses to run faster and get money quicker. Hence, officials must be able to provide good services by running all their processes more efficiently, without any rent-seeking activities, which are regarded as specific characteristics of infrastructure projects (Davidson, 2010).

In the reformation era, the involvement of the private sector in public-sector projects is widespread, whereas in the previous era it only involved a small number of private sector individuals who were close to the political elite. Engagement of the private sector in public-sector business is still needed, as the infrastructure is still considered undersupplied and serviced. Involvement of the private sector in infrastructure projects can be accommodated through PPP (Public-Private Partnership) schemes (Tirtosuharto, 2012; Chen et al., 2013). In the LoI of October 31st, 1997, the IMF suggested creating a competitive environment via a privatisation policy and the involvement of the private sector in infrastructure schemes, such as building roads,

bridges, irrigation, power supply works etc. In order to ensure competitiveness, the government set guidelines for procurement and contracting procedures, which were formally issued at the end of December 1997. Moreover, the guidelines indicated the important role of government in stimulating the growth of private enterprises, especially small to medium enterprises (SMEs), which are perceived as the catalysts of economic growth in developing countries (Tirtosuharto, 2012). The commitment of central government to the realisation of the competitive environment is supported by the Ministry of Finance, which plays an important role in regulating fund disbursement and the accountability of that disbursement. The MoF is also supported by the BPKP, as the government's internal auditor, the BPK, as the supreme audit that has authority to give an audit opinion, the KPK, as the anti-corruption commission, and the Tipikor court, as a special court in cases of corruption or bribery that occur during the procurement processes. Such broad support will serve to maintain the competitive environment that has been suggested by the IMF. If any government officials are found to be involved in corruption or receive bribes, the Ministry of Empowering of State Apparatuses will take responsibility for punishment, based on civil servant regulations.

Involvement of the private sector is not only a matter when undertaking a project as vendors or suppliers; some ministers are recruited from the professions or from the private sector. Being a bureaucrat was a prestigious position to have during the previous regime, and was always protected by the President. However, nowadays many professionals from outside the government have been placed in the top-tier management of ministries, as such individuals are expected to bring new ideas, new paradigms and a fresh attitude to public-sector organisations, in terms of how civil servants should do their work professionally, provide services responsibly, and be market-orientated and with a focus on the customer. Thus, the government institution is expected to be able to support both the business community and the public as consumers, because top managers in the private sector are regarded as having the expertise to support and facilitate improvement in the public sector (Potrykus, 2010).

The injection of 'new blood' into the system is perceived as being the only way to change the dominant, somewhat self-interested and irresponsible, culture in public administration, which does not focus on providing effective and efficient public services. Moreover, this view is also in line with suggestions from the World Bank in terms of efforts to accelerate the reformation of Indonesia's public service. Although it cannot fully eliminate bribery or rent-seeking practices in public-sector organisations,

nowadays the civil servant's mindset has been considerably changed; and, as a consequence of these changes, the bureaucrats are also treated as equivalent to professionals in the private sector by increasing their benefits and remuneration.

2.4.4. Impact on Strengthening Civil Society

In the LoI, the IMF also set an agenda to empower civil society in Indonesia, because it is perceived as one of the most important dimensions of development, along with the government and the private business sector. Civil society was suppressed by the prior regime, as all movements such as labour unions, student unions etc. had been controlled by the state. Hence, civil societies need to be empowered after the fall of the previous authoritarian regime. Although there is no consensus about the term *civil society*, it can be defined as following:

Civil society is understood as the home of enlightenment values like individualism, personal liberty (and property), and rationalism (if not secularism), and more politically, of human rights. Civil society organisations are then guardians of this treasure, and advocates for such values in the state and economy. (Harney and Olivia, 2003)

One of the attempts of government to educate society is through the involvement of the press, such as to communicate policy via mass media. This effort builds public trust in the government on one side, as the public is provided with many perspectives and is acquainted with the rationales behind the policy, which in turn enables the public to observe the implementation of the policy. When the policy works well, the public will then hopefully give it a positive response and their support. The role of the press, in the era 1998-2000, was vital for the support of democratic movements, which led to the downfall of the autocratic regime and encouraged the adoption and development of the democratic process. Therefore, the role of the press was crucial to disseminate the desired messages. However, currently, the press is still focusing on the upper and upper-middle classes located in the metropolitan area (Hollander et al., 2009).

In Indonesian culture, the public must be re-assured by evidence. If they are offered many concepts, they will not believe them unless they are presented with clear evidence that they work. Moreover, the public also needs role models, then they will follow their lead; otherwise, they will reject what is being offered or presented. Therefore, empowering Indonesian civil society should begin mostly with intellectuals, who come from universities, or social organisations, such as the two religious-based

organisations NU (Nahdlatul Ulama) and Muhammadiyah, which tend to be more independent and have support from 'grass roots' people – in other words, from the public domain, and not necessarily managed by the government (Tornquist, 2006). These religious organisations are the largest mass-based Islamic movements, having more than 70 million affiliates all over Indonesia, and are regarded as major civil-society players (Fuad, 2002). Each organisation has a different mass base: the majority of Muhammadiyah's members come from the urban middle class, while the NU has its base in rural and traditional communities; however, both of them have the same concerns (Barton, 2014). These organisations actively engage in anti-corruption training and workshops, and outreach through mass media (Setiyono and McLeod, 2010).

Another way to develop civil society in Indonesia is by developing CSOs (Civil Society Organisations). The CSOs engage with government to meet their specific agendas fulfilling numerous roles such as watchdog, facilitators of government, or advocates (Antlov et al., 2010; Setiyono and McLeod, 2010). Some CSOs have developed formal structures and have the remit to educate members of the public on combating corruption; these include ICW (Indonesia Corruption Watch), MTI (*Masyarakat Transparansi Indonesia*, Indonesian Society for Transparency) and IPW (Indonesia Procurement Watch), which flourish because they have been triggered by the democratic transition (Setiyono and McLeod, 2010).

However, the development of CSOs has not run smoothly for a number of reasons. First, civil society organisations have been used as political vehicles, either religion-based or ethnic-based. The second reason is the distrust between the CSOs and politicians that has built up in parliament. The CSOs suspect politicians of being a group of corrupt people with no interest in empowering society. At the same time, the politicians see that CSOs receive financial support from abroad, and believe that they are designed to discredit Indonesian political systems, because in the first decade of the reformation era some CSOs received considerable funds from donor agencies to transform themselves into formal organisations in order to undertake their programmes on governance and anti-corruption activities (Setiyono and McLeod, 2010). Third, most of the CSOs still deal with internal factors. For example, they implement confrontational strategies because of the CSOs' leaders have limited political skills, limited organisational capacity and inability to articulate the interests of indigenous societies to policy makers. Politicians also address CSOs' sustainability issues, i.e. the

social and cultural gap between the CSOs and general society (Antlov et al., 2010). Fourth, the holders of power are mainly concentrated in a combination of private sector and state interests: 40% relate to public executives, 16% is in the hands of the police and military, 17% in parliament and political parties, and 12% is related to business or CSOs. Moreover, weak representation and the dominance of influential actors and the middle class in parliament further weaken the role of the public in general (Tornquist, 2006).

Another form of participation of local society in local government is expressed in political sector, where central government facilitates direct elections both of the head of local governments and local parliament members in every region (Tornquist, 2006; Bennet, 2010). However, the awareness that local society has of the political and economic aspects of government is still low. Hence, without educating people to raise their awareness (Schutte, 2012), local society will only become a legitimating tool, because public participation is more ceremonial than genuine, and only serves to fulfil the regulation requirements (Purba, 2010; Sopanah, 2012). Local society can easily be manipulated by political elites to achieve their political ambitions.

2.5. Issues over Public Expenditure Control and Capital Expenditure Control in the Post-Reformation Era

Based on these conditions described in the previous sections, many studies have been undertaken to investigate the process and effects of decentralisation as listed in appendix 6, such as (Ridha and Basuki, 2011; Mustafa et al., 2011; Amirya et al., 2011; Nugraha, 2010; Djamhuri, 2009; Rahmanurrasjid, 2008; Harun, 2007; Abdullah and Asmara, 2006; Cameron et al., 2005; Sumarto et al., 2004; Alatas et al., 2002). Several of these studies focus on financial control in Indonesian local government from many perspectives, such as opportunistic behaviour from the agency theory perspective (Abdullah and Asmara, 2006), as well as some studies on the importance of internal control in local governments (Nugraha, 2010; Mustafa et al., 2011). In addition, research based on institutional theory with various focuses have been carried out, such as emphasising budgeting and accounting systems (Djamhuri, 2009; Amirya et al., 2011) and underscoring the impact of external pressures, uncertainty, and management commitment to transparency in the financial reporting of local government (Ridha and Basuki, 2011).

Abdullah and Asmara (2006) investigate how the legislative body use government regulations as a foundation to behave opportunistically for its own benefit; their study which covers 53 local governments (cities and districts) as samples. Findings of this study indicate that legislative members behave opportunistically towards budgeting processes, which are affected by *Pendapatan Asli Daerah* (local government income) and the *Anggaran Pendapatan Daerah* (local government budget) as mediums for corruption. Meanwhile, studies on the internal control of local government have been performed on Indonesian local governments as well, such as Nugraha (2010) on the Provincial Government of West Java and Mustafa et al. (2011) on Kendari City. All of these studies indicate the importance of an effective internal control system to ensure the reliability of financial information. In addition, Mustafa et al. (2011) find that technology is required to enhance the reliability of financial information, and that human resources are insignificant factors, because of the insufficient knowledge of the staff in accounting.

Other research is conducted by Amirya et al. (2011), referring to the study by Djamhuri (2009). Amirya's study selected Brawijaya University as the research sample, while Djamhuri employed a local government as his sample. Both of them apply institutional theory as a lens through which to investigate budgeting and accounting practices in local government or in state-owned enterprises. Djamhuri (2009) investigates performance-based budgeting and accrual accounting in a local government. His findings indicate that introducing a new budgeting and accounting system will cause decoupling due to the insufficient quantity and quality of staff in accounting, and the rigidity of bureaucratic culture. Meanwhile, Amirya's findings indicate that the adoption of budget and accounting systems is required to compile all regulations for state university, such as Brawijaya University. Another research based on institutional theory is performed by Ridha and Basuki (2011), investigating some factors affecting transparency in financial reporting. They emphasise isomorphism methods, i.e. coercive, mimetic, and normative, on the transparency of financial reporting; their findings indicate that implementation of financial transparency is affected by external pressures which are imposed through laws and regulation from central government and by management commitment.

Referring to the findings of those studies (Abdullah and Asmara, 2006, Djamhuri, 2009, Nugraha, 2010, Amirya, 2011, Ridha and Basuki, 2011, and Mustafa et al., 2011), control mechanisms are required, but there are still some internal and

external local government issues. The quality of local government finance staff is still regarded as an internal obstacle, according to Djamhuri (2009). Meanwhile, the external obstacles include the opportunistic behaviour of local parliament members (Abdullah and Asmara, 2006), who use the rigidity of bureaucracy (Djamhuri, 2009) that requires compliance with many regulations (Amirya et al., 2011, Ridha and Basuki, 2011) to facilitate attempts at rent-seeking.

Furthermore, regarding the study of capital expenditure in local government, much research has been undertaken with samples from many regions, such as in Java and Bali regions (Harianto and Adi, 2007); in Central Java province (Nuarisa, 2013); in West Java Province (Arwati and Hadiati, 2013); in Bali province (Jaya and Dwirandra, 2014); and in Central Sulawesi province (Oktora and Pontoh, 2013). Most of these studies investigate factors affecting the allocation of capital expenditure by local governments. The findings of these studies vary: for example, Abdullah and Halim (2006) suggest that the allocation of capital expenditure in 32 local governments in Sumatera Island is affected by income from central government, i.e. DBH, DAU and DAK (Abdullah and Halim, 2006). This conclusion is confirmed by Harianto and Adi (2007), who study the financial structure of local governments located in the Java and Bali regions. Their findings indicate that DAU positively affects the allocation of capital expenditure, which stimulates the increase of PAD; a conclusion which is in line with the studies by Nuarisa (2013) and Jaya and Dwirandra (2014). However, this finding contradicts the study by Arwati and Hadiati (2013), who find that DAU does not affect capital expenditure decisions; while another study indicates that DAK does not affect the allocation of capital expenditure (Darmayasa and Suandi, 2014).

Concerning the role of PAD in determining the allocation of capital expenditure, Abdullah and Halim (2006) find that local government still rely on income from central government instead of local income (PAD). This finding is consistent with the studies of Wandira (2013), Oktora and Pontoh (2013) and Darmayasa and Suandi (2014), whose studies all indicate that PAD does not affect the allocation of capital expenditure. In addition, regarding the economic growth of local government, Harianto and Adi (2007) find that income per capita negatively affects allocation of capital expenditure because local governments tend to reduce the proportion of capital expenditure when they have met the target of local income per capita (Jaya and Dwirandra, 2014). This finding is not confirmed by Arwati and Hadiati (2013),

however, who conclude that economic growth does not affect allocation of capital expenditure.

Apart from research concerning factors affecting capital expenditure decisions, there are several studies focusing on control mechanisms in local government embracing internal and external factors. One has been undertaken in the Talaud Island district, suggesting that local government has formed its financial statement based on government accounting standards, but that local government does not provide stakeholder access to that statement (Poe and Saerang, 2013). Consequently, the transparency and accountability of financial management of local government are perceived as weak. Another study is undertaken by Mogi and Morasa (2013) in the District of Sangihe Island, based on 2011 data, which has had a 'disclaimer opinion' from the BPK, as Indonesia's supreme audit, for the fiscal year of 2011. Their findings indicate that the local government acquire lands as fixed assets, but these are not supported by any legal evidence of ownership in the form of land certificates, which in 2010 identified 107 land parcels valued at over IDR16 billion or equal to USD1.1 million (assuming USD1 = IDR14,000). Moreover, this study also finds many assets from central government that have not been recorded and recognised as assets of local government (Mogi and Morasa, 2013). Syafitri's (2012) study also emphasises internal factors in a local government, the city of Palembang, South Sumatra, where, it is suggested, the city manages its financial recording based on government accounting standards, but still does not take into account depreciation of assets and accumulation of depreciation. Consequently, there are many discrepancies that occurred between real conditions and the value of fixed assets – particularly fixed assets that have almost reached the end of their economic life, because fixed assets are still recorded and recognised based on their acquisition cost (Syafitri, 2012).

Meanwhile, several studies regarding external factors of control mechanisms have been undertaken by Nuru et al. (2013) in the city of Sorong focusing on local parliament members; the researchers conclude that local parliament members still lack knowledge of budgeting mechanisms. Another finding indicates that any involvement of local society is merely symbolic, and occurs only to comply with government regulations (Nuru et al., 2013). Another study on external factors by Wonda et al. (2013) in Puncak Jaya district investigates factors affecting local parliament to perform control mechanisms on the local budget. Their first finding is that the placement of a local parliament member into a particular commission, which is responsible for control

of the local budget, is based on the recommendation of a particular political party, instead of the background of the member. Second, parliament members from coalition parties will have dominant roles regarding the formulation and ratification of local budgets, rather than opposition parties. Third, about 87.5% of local parliament members do not have comprehensive knowledge about the regulations of financial control mechanisms (Wonda et al., 2013).

Referring to these findings from the cited studies in capital expenditure, several issues can be highlighted: first, recording and recognition of acquired fixed assets; second, legal evidence of ownership; and third, accessibility to local government financial statements. In addition, control from other parties, such as local parliament, is still weak because of the dominance of political parties over local parliament members and the lack of knowledge of local parliament members, particularly regarding issues relating to financial control mechanisms. Input from local society is also weak because it is merely symbolic in nature and occurs only in order to meet the requirements stipulated by regulations. In summary, from a general perspective regarding the financial management of local government and the specific perspective on capital expenditure, there are several issues on control mechanisms that encompass both internal and external parties that can be investigated further in order to get an understanding of the whole picture of control mechanisms in Indonesian local government.

2.6. Summary

This chapter is intended to give an overview of the financial, governance and civil service reform in Indonesia, which mainly relies on secondary sources. Although the engagement with the IMF raised pros and cons between ministers, the IMF has brought new values to the GoI, which has since affected the way that the GoI runs the government. However, the values that have been introduced do not fit entirely with Indonesian culture. Several points can be underlined derived from this chapter related to factors affecting those reforms that subsequently will affect lower levels of government. The first refers to the involvement of three ministries in regulating local governments. The Ministry of Home Affairs is responsible for nation building and the regulation of decentralised governance, political systems, regional development and

community empowerment; the Ministry of Empowerment of State Apparatus and Bureaucratic reform regulates civil servants along with the services they are expected to provide; and the Ministry of Finance deals with fiscal balances and financial transfers to local government. All government institutions are interrelated and influence each other. However, there is still a lack of coordination and communication. For example, a lack of coordination at ministerial level in producing ministerial regulations might contradict or have the same substance as regulations issued by another ministry, which in turn may affect local government agencies and compound problems regarding the implementation of the regulations at local government level. In addition, local governments are not only regulated by the Ministry of Home Affairs (MOHA), the Ministry of Finance (MOF) and the Ministry of Apparatuses Empowerment and Bureaucratic Reform, but must also adhere to regulations from related ministries. Ministerial coordination and regulation are perceived as being related to departmental or ministerial ego, in which every ministry might issue ministerial regulations to look after their own interests.

The second is the involvement of citizens in monitoring programmes; this is an initiative which can be established through civil-society organisations based on commonality of society and non-government organisations, either local or internationally affiliated NGOs. The third, which is interaction between government and CSOs, can be facilitated by political parties, each of which will have their own agendas. Fourth, the private sector has been facilitated through the establishment of a competitive environment and support from government for facilitating the engagement of private sector businesses in infrastructure projects. Finally, the GOI endorses the involvement of professionals from the private sector into ministerial-level positions.

Several issues related to the internal aspects of local government can also be identified within this chapter. The first is the lack of ability of government officials, as a result of which conditions become severe when central government heightens the standard of transparency by requiring various reports to be available, and for public spending requirements to be fulfilled. On the other side, as those responsible become more important, central government provides higher remuneration and benefits for the government officials, although there are still pros and cons regarding the policy. The second is the low involvement of society in the social control of government and parliament. The third is the wide span of central government's control and the empowering of provincial-level government to cope with the lack of coordination between central and municipal government. The fourth factor is political influence on

government, and ensuring the capacity and independence of heads of government institutions to resist the interference of political influence. The last factor is dealing with local culture. For example, the role of head of a government institution is very important, especially as a role model in his/her organisation, thus, he/she must be able to be a leader in the organisation. Particularly in Indonesian culture, the leader is given a higher status and is perceived as a master or lord. This culture is still sustained by the organisation's members. Therefore, the leader tends to be authoritarian. To sum up, these findings consistent with the study of Faquet (2013), indicating that issues on decentralisation are related to the lack of political will, low bureaucratic ability and insufficient resources.

After the context of this study has been described in this chapter, the following chapter discusses the theoretical basis and research method applied in this study.

Chapter 3

Control Mechanism within Foucauldian Perspective

3.1. Introduction

The previous chapter described the context of this study, focused on the introduction of new values to the Indonesian government by international institutions that had both positive and negative implications. Introducing new values from another, different culture affects the dynamics of the organisation, it is suggested (Bourne and Jenkins, 2013). Likewise, as international institutions introduced new values, this affected the dynamics of the Indonesian public sector, especially on establishing control mechanisms in capital expenditure, both in central and local government.

This chapter now elaborates on how those values influence the implementation of control mechanisms in an organisation. In this stance, control is perceived as a focal point in management processes apart from planning and organising activities. It is a required mechanism for conducting actions effectively and accountably, which are provided by control and control techniques. These control mechanisms are related to individual human interrelation, which requires the individual to adhere to an arrangement. The control mechanisms have evolved from emphasising power in the early stage to subsequently emphasising behaviour, and then involving multidimensional aspects (Belkaoui, 1986). Miller and O’Leary suggest shifting perspectives: from seeing the individual as a machine to treating an individual as a decision-maker. This points to the importance of the personal dimension in control mechanisms, because the individual has opportunity to make choices, include in relation to the acceptance of norms, instructions, and standards. Hence, every management tool should consider the complexity individuals along with their needs and objectives (Miller and O’Leary, 1987).

In addition, this chapter provides viewpoints for conducting and analysing a case study whose findings are set out in the following chapters. Accordingly, this chapter is structured as follows: the first section is an introduction; this is followed by a description of the control systems in an organisation. This second section covers control systems, various approaches to control, and the cultural aspects of control. Then, the third section describes control as a form of responsible accounting, where an individual is required to take responsibility for the resources under his/her control. The fourth section discusses the roles of power and knowledge in control systems. The subsequent section covers the application of discipline and surveillance in control systems. Then, referring to the analysis provided the preceding sections, the discussion shifts to the research methodology and design, which become the basis for determining the approach of this study, i.e. the justification for applying a particular research method and case-study approach in this research and determining the data-collection method. Finally, the content of this chapter is summarised in the section summary.

3.2. Control Systems of an Organisation

Control systems are divided by Merchant and Stede (2012) into two basic functions, i.e. strategic control and management control. Strategic control is considered to be “something that makes an organisation unique; a winner or a survivor” (Thomas

1993, p.3 as cited in Coad, 2005, p.168). Strategic control can be further categorised into two functions: the first ensures that an organisation's strategy, i.e. what it determines to be its long-term goals and objectives, is on the right track, indicated by specific short-term goals (milestones) (Langfield-Smith, 2006; Berry et al., 2005a); the second ensures the relevance of that strategy by considering changes within the business environment through systematic and continuous surveillance of internal and external factors (Coad, 2005; Simons, 1995; Langfield-Smith, 2006). The strategic control function was developed predominantly in the 1960s to the mid-1980s, referring to the work of Robert N. Anthony (1965), who proposed how important it is for an organisation to apply strategic planning, management control and operational control (Belkaoui, 1986). Similarly, management control was defined by Anthony in 1988 as the process by which managers influence other members of the organisation to implement the organisation's strategies through formal, information-based routines and procedures (Cowton and Dopson, 2002). The function implies that the management control system acts as an intermediary between strategic control and operational/task control that is employed in a stable environment and in mechanistic organisations (Langfield-Smith, 2006; Coad, 2005; Berry et al., 2005a). Operational control is closely related to day-to-day activities in an organisation, and must carry out its tasks in an efficient and effective way (Berry et al., 2005a).

The formal routines and procedures of management control systems encompass plans, budgets and market-share monitoring systems; information-based systems provide up-to-date information for all organisation members regarding emerging developments (Simons, 1995). Concerning information flow, control systems also cover both vertical and horizontal information. Control systems also cover reporting structures, such as performance reporting and incentive systems (Langfield-Smith, 2006). The information should encourage and facilitate all levels of the organisation in searching, learning, and innovating in response to environmental changes (Simons, 1995).

One of the important aspects of the formal set of procedures and policies is the internal control system, which is intended to reduce fraud by safeguarding assets and ensuring the reliability of financial statements by producing accurate accounting systems (Edmonds et al., 2011; Simons, 2000; Leitch, 2008). In the early development of internal control systems, attention was purely focused on bookkeeping, i.e. on checking and detecting whether bookkeepers were making any errors or committing

fraud. However, following recent developments, the coverage supplied by internal control has been extended to embracing business risk management (Leitch, 2008), as set out by the Committee of Sponsoring Organisations (COSO) in the five characteristics or components of internal control systems: (i) the controlled environment, i.e. the foundation of all other components of internal control; (ii) risk assessment, meaning the identification and analysis of risks that might emerge from efforts to achieve the entity's objectives; (iii) control activities, involving processes, policies, and procedures to ensure the accomplishment of management directives; (iv) information and communication, consisting of systems and reports to support management and help employees to undertake their responsibilities; and (v) monitoring, i.e. activities intended to supervise the internal control performance of those within an organisation (Woods, 2008; Graham, 2008).

In addition to the concept of formal control, Langfield-Smith (2006) indicates that management control systems also involve informal controls, encompassing performance measurement systems, employee and managerial incentive systems, physical controls over assets, personnel controls, and cultural and social controls. Hence, organisations must set up feasible mechanisms to induce all organisation members to pay attention to accepted behavioural aspects. Without such control mechanisms, members of an organisation or business might initiate uncoordinated activities that can lead to financial failure, reputation damage, and/or, even worse, organisational failure (Berry et al., 2005b; Merchant and Stede, 2012). Consistent with this perspective, Turnbull Guidance³ (2005 par. 19) suggests that it is important to consider behavioural aspects to ensure that an organisation's control systems protect assets and manage risks (Kajuter et al., 2008).

3.3. Various Approaches of Control Mechanisms

Control involves interrelationships between an organisation's members, both vertically, in superior-subordinate relations, and horizontally, with colleagues. Control starts at the beginning of the business process, and neglecting one element of the business process will affect the strength and degree of control (Follett, 1932). Furthermore, Ouchi (1979) describes a control mechanism as the surveillance and

³ Internal Control: Guidance for Directors on the Combined Code (the Turnbull Guidance) was first issued in 1999. In 2004, the Financial Reporting Council established the Turnbull Review Group to consider the impact of the guidance and the related disclosures and to determine whether the guidance needed to be updated.

directing of subordinates by their superiors, together with the introduction and implementation of rules concerning processes or standards of quality and quantity (Ouchi, 1979). Sometimes, a control mechanism places more emphasis on monitoring, evaluating, coercion, and oppression; this is an orientation which prompts unenthusiastic responses from employees because such a model is perceived as an insult to their sense of autonomy and self-control (Macintosh and Quattrone, 2010; Ouchi, 1979).

Organisations can choose many differing control mechanisms, as suggested by Ouchi and Merchant, which can involve action (behavioural) control, personnel and cultural (or clan and social) control, and result (or output) control (Drury, 2001). However, having more controls does not guarantee a better quality or standard of control (Merchant and Stede, 2012). Action control ensures that the actions of every organisation member are beneficial to their organisation; personnel control motivates all organisation members to perform tasks on their own; and cultural control shapes organisational norms and encourages employees to monitor and influence each other's behaviour (Merchant and Stede, 2012). Meanwhile, result (output) control is seen as a system that requires monitoring to compare the output of processes to determine targets and then make adjustments or take corrective actions if the output deviates from the target (Pidd, 2007; Drury, 2001).

Choosing particular control mechanisms must be based on the context, values, and beliefs of an organisation, because each condition requires different types of control (Follett, 1932; Scheytt and Soin, 2005; Edmonds et al., 2011). Different parts of an organisation may behave differently even though theoretically they are guided by the same control system (Berry et al., 2005b). Therefore, those designing a management control system must consider the expectations that an organisation has of their employees in order to conceive the strategies and objectives of that organisation, which will subsequently reduce the occurrence of behavioural problems, helping to prevent any unpleasant surprises (Merchant and Stede, 2012). This notion is consistent with Follett's idea of two points of control design, i.e. the focus on fact-control instead of man-control, and on the correlation between many controls rather than the adoption of one superimposed control (Follett, 1932).

Furthermore, designing a control system must encourage an organisation and its members to adapt and respond to environmental changes in order to enable strategic

responses (Langfield-Smith, 2006). Hence, the environment is considered as very important, because it has integrity and involves many kinds of qualitative ethical issues, governance and management styles, accounting and business competencies, and personnel policies and human resources (McPhail, 2005; Graham, 2008). Likewise, the environment must be assessed carefully because it is intangible and subject to interpretation and rationalisation (Graham, 2008). Therefore, there is no such thing as a perfect control model or system; even good management control still allows for some probabilities of failure (Merchant and Stede, 2012).

Another approach to the mechanism of control involves informal processes that affect the behavioural aspects of employees' performance, because a rigid, top-down, command-and-control technique is not an appropriate fit in a competitive environment that requires creativity and initiative from its employees. Application of organisation control tends to provoke various responses, including resistance (Cowton and Dopson, 2002). Therefore, the control model needs to strike a balance between top-down direction and bottom-up creativity, between surveillance and feedback systems, and between command control and social and cultural controls (Simons, 1995; Merchant and Stede, 2012). Regarding social control, Hopwood (1974) suggests that this reflects social perspectives or norms and patterns of social interaction (Berry et al., 2005a). Meanwhile, cultural control offers mutual monitoring of those who wittingly or unwittingly violate group norms and values; it is the most effective control model when a group has social or emotional bonds (Merchant and Stede, 2012). Cultural controls embrace the values, social norms and beliefs that are shared by an organisation's members and influence their behaviour; it is a model that requires all members to understand their roles, and the capabilities needed to undertake those roles. Therefore, personnel or cultural controls are suggested as optimal because they have fewer side effects, are relatively unobtrusive, and incur lower costs as well. However, personal or cultural control models are usually combined with other forms of controls. Hence, if the personal or cultural control models do not fit with the conditions of an organisation, it is necessary to assess the reliability of the chosen control system and the possibility of employing and applying other forms of control (Merchant and Stede, 2012; Drury, 2001).

3.4. Cultural Approach to Control Mechanisms

An organisation binds individuals who have the ability to identify opportunities and convert them into an output of value, along with available resources based on specified objectives (Simons, 1995). Dynamic interaction between individuals affects social and organisational situations, during which they learn about the consequences of their actions. They also share concepts of structural stability – depth, breadth, and patterning of integration – which are less tangible and less visible; this pattern is known as organisational culture. This culture also consists of shared traditions and sets of structures, beliefs, values, ideologies, routines, rules and norms, all of which inform members on how to behave in an organisation. This behaviour is shaped by words and by example, including leadership behaviour, codes of conduct, employee rotation, group rewards, and physical and social arrangements (Schein, 2004; Scheytt and Soin, 2005; Merchant and Stede, 2012).

Organisational culture is also perceived to be a representation of the common perceptions of an organisation's members implied in the relational and internal processes of the organisation. Chatman and Jehn (1994) describe organisational culture as being based on seven primary characteristics that exist in every organisation, i.e. innovation and risk-taking, attention to detail, outcome orientation, people orientation, team orientation, aggressiveness, and stability. Therefore, an organisation is considered to be a complex cultural entity (Scheytt and Soin, 2005); any attempts to change it are regarded as a threat because culture implies some level of structural stability in the group (Schein, 2004; Ouchi and Wilkins, 1985).

Managers' nationality and the business environment influence an organisation's values, because managerial work essentially focuses on the social and political rather than the fundamentally analytical (Silverthorne, 2005; Watson, 2012). Therefore, as a form of managerial responsibility, a manager has to ensure that organisational activities conform to the organisation's strategies through administrative and cultural mechanisms (Simons, 1995). Culture is not perceived as a key factor of success, but it is essential for all of the organisation's members to gain a perspective on organisational processes and understand the nature of organisational life (Scheytt and Soin, 2005). Hence, a strong cultural component of an organisation affects the level of organisational control. This level of control decreases when an organisation's beliefs and norms become highly institutionalised. However, a culture becoming 'too strong' has a negative effect because it is difficult to adapt when the environment changes rapidly (Merchant and Stede, 2012), causing an inevitable interaction between

organisations and their environments (Peter, 2000; Meyer, 2008). Hence, any changes in the business environment require organisations to adjust their formal structure, organisational structure, and goals, programmes, or missions (DiMaggio and Powell, 1983).

The effectiveness of a culture is determined by its interaction with its environment, which influences all aspects of the organisation, either official or unofficial. Dimensions of this mingling can be seen in certain issues such as primary tasks and internal operations, rituals, climate, artefacts, jargon, stories, jokes and humour, legends, myths, sagas, rewards or punishments, and behaviour (Schein, 2004; Merchant and Stede, 2012; Watson, 2012; Scheytt and Soin, 2005). However, each organisation has different ways of responding to its environment, because the culture and societies of the organisation vary either locally and/or nationally. Therefore, research in international settings shows that the application of a particular management technique in one culture does not always produce the same result in another culture (Silverthorne, 2005).

3.5. Control as a Form of Responsibility Accounting

Management control systems (MCS) are closely related to financial data, which have put accountants in an important position for ensuring the effective operation of organisations by applying two components: first, establishing effective control through directing the activities of subordinates; second, evaluating the outcome of activities and deciding on corrective actions if required (McNally, 1980). The latter are affected by managers' past experiences, organisational history, and commitment to delegating control (Choudhury, 1986). Furthermore, McNally (1980) argues that accounting still emphasises the second component and neglects the first component, although both have the same importance from an accounting perspective. There are two reasons for the importance of the first component: (i) designing and operating the MCS requires an understanding of the distribution of control in an organisation; and (ii) the authority to control is outlined in an organisation's formal structure, rather than relies on the influence of an organisational member in an organisation. The formal organisation system and standard operating procedures are beneficial for accounting in order to identify the centre of responsibility, resource utilisation, and decision-making (McNally, 1980).

The MCS is designed and implemented by accountants based on the principles of responsible accounting, characterised by the controllability principle (McNally, 1980; Choudhury, 1986; Antle and Demski, 1988), i.e. “personnel within the system of budget should be charged or credited only for items within their control” (McNally, 1980, p.165), or, in other words, can be expressed as “control begets responsibility” (Antle and Demski, 1988, p.714). Hence, responsible accounting only focuses on costs incurred under a manager’s control; any ‘external’ influences should be eliminated (Choudhury, 1986). Furthermore, Choudhury (1986) suggests three types of controllability filters: event separation filters; manager separation filters; and period separation filters. Event separation filters suggest that a manager’s performance should not be affected by any events outside of his/her control. A manager separation filter demonstrates the importance of separating a manager’s performance from effects resulting from the actions of other managers: for example, a manager’s operating decisions might be related to investment decisions made by his/her superior, which are beyond the manager’s control. Finally, the period separation filter indicates the exclusion of any effects on current decisions derived from the past (Choudhury, 1986).

Referring to the principle of controllability, it is necessary to distinguish between controllable and non-controllable costs based on authority that has been prescribed in a formal organisational structure. Understanding the two components of the cost is needed for several reasons: (i) if someone responsible for costs under his/her control, it generates a positive attitude and cost awareness; (ii) the inclusion of non-controllable variables in performance assessment produces an unfavourable response; (iii) sometimes, a manager is required to be accountable for variances in non-controllable costs or items by a superior; (iv) the combination of budget constraints and non-controllable items tends to intensify tensions, and later affects decision-making behaviours that tend to avoid innovation and adopt low-risk strategies (McNally, 1980).

In order to overcome these conditions, McNally (1980) suggests three possible structural changes. First, he suggests identifying varying degrees of control over items or costs, which will then generate three, four or five levels of control instead of only two categories, controllable and non-controllable. This idea is based on the concept that degrees of control can be perceived as a continuum. Second, he suggests emphasising control over areas of activity or decisions, because a manager might participate in different activities involving different levels of control, particularly in collaboration with other departments. Finally, he suggests broadening the interpretation of control by

suggesting that formal authority should consider informal organisational influence. Informal organisational influence affects responsible accounting in several ways; for example, a resource may be located within a department, but control over the resource is outside the manager's control, and so should be excluded from the accounting report responsible (McNally, 1980).

Management control still assumes that managerial legitimacy is being taken for granted, meaning the organisation as a unitary entity, and neglects issues of power and conflict. Anthony even argues that in the absence of power, authority is still present, because strategies have been determined and implemented through assignments. Hence, development studies on management control are focused on the development of a critical perspective on management control, particularly power issues. This brings in Foucault: although Foucault's works are not directly related to management or accounting, they have influenced studies on these fields (Cowton and Dopson, 2002).

3.6. Roles of Power and Knowledge in Control Mechanisms

Macintosh (1994) suggests five paradigms of accounting theory, i.e. structural functionalist, interpretivist, radical structuralist, radical humanist, and postmodernist; these are described in turn. The first paradigm, structural functionalist, also known as rational contingency, relies on empirical works which apply a natural sciences approach to analysing how organisational control works. This paradigm begins with a hypothesis, quantitative data and statistical analysis; hence, it is perceived to be more neutral and objective than the others. The second paradigm is interpretivist or subjective interactionist; this emphasises the interaction between members of an organisation, and holds that there is no single objective approach to organisational reality. However, this paradigm perceives that an approach to organisational reality is determined by a personal interpretation of certain situations. The third paradigm is radical structuralist, offering a similar view to structural functionalism, i.e. assuming that an organisation as a social system has a concrete ontological existence. However, it emphasises the existence of parties who hold the power to rule and exploit the other members of the organisation. The next paradigm is radical humanism, which assumes that there is a subjective social world with a people-oriented view. This paradigm has enlightenment and emancipation aims. The enlightenment aim is about encouraging the self-induced awareness of organisational members, while the emancipation aim is

intended to increase the power and responsibility of the self-constructed social structure. The last paradigm is postmodernism, which arose in opposition to dominant paradigms in accounting theory, such as structural and radical functionalism. This paradigm encourages marginalised parties to create their own discourses in resistance to hegemonic power (Macintosh, 1994). In a different context, Foucault expresses it as “an instrument for those who fight, those who resist, and refuse what is” (Harris, 2001). Postmodernism regards discourse as a method to observe, monitor, shape, and control behaviour, compelling individuals to act as expected. Hence, individuals’ behaviour will become predictable, and large bodies of people can thereby be managed (Cowton and Dopson, 2002). Developing discourses, also known as regimes of truth, are attempts to treat humans as objects of study, examination, diagnosis, and correction. A regime of truth might contain various discourses and knowledge that are perceived by particular society as true. Each regime of truth derives its own criteria that are used by its members to distinguish between true or false values. The regime of truth cannot be separated from power relations in order to determine strategies of social interactions because of the power relation build-up structure of social interaction (Macintosh, 2002).

Power will be prominent when challenged by other parties because power is applied to others’ actions or “an action upon action on possible or actual future or present actions” (Foucault, 1994, p.340). Furthermore, Foucault perceives power as omnipresent, an endless and open strategic game (Gordon, 1991). Foucault (1994) also indicates that power tends to be more repressive, although in some sense it is also considered productive. Likewise, power that is viewed solely from the perspective of political science contributes a narrow perspective, as it only focuses on power in the public domain and ignores invisible sets of practices (McKinlay and Starkey, 1998).

Power is perceived as a way to direct individuals or groups to embrace many approaches, ensuring their subjection to political or economic ideas in order to “structure the possible field of action of others” (Foucault, 1994). The ‘subject’ gives up his own identity consciously, and is put under the control of someone else because of economic and social processes as a form of subjectivity. Hence, the mechanisms of subjection can be identified based on their relationship with mechanisms of exploitation and domination (Gunn, 2006). This is perceived as a manifestation of power, which people need to exercise over others, as power is designed in relation with ‘partners’. This power relationship consists of two elements: first, the *other*, who is recognised and maintained as a subject; second, through *conduct*, which means to lead the *other* based

on mechanisms of coercion and the exercise of power (Foucault, 1994). This domination can be described as a stable and hierarchical relationship resulting from technologies of government that give subordinates extremely limited space to manoeuvre (Lemke, 2002).

Meanwhile, from Gramsci's perspective, power is conceptualised as 'hegemony' that tends to be exercised through the channels of intellectual and moral capacity rather than by coercion, and is perceived to be more complex than the propaganda and manipulation method. Hegemony embraces the realities of the politics, economics, and social structure of the masses, and involves negotiation between the dominant and dominated because the interests of the masses tend to change from time to time (Gunn, 2006). Gramsci, in Lemke (2007, p.51), suggests that the state cannot be perceived as being a result of a compromise between classes, gender or other groups, but as a strategic articulation (Lemke, 2007). As indicated by Lukes, in Gunn (2006), there are three different views of power; these are categorised as the one-dimensional view, involving visible conflict, the two-dimensional view, involving visible and latent conflict between parties with conflict of interest, and a three-dimensional view, which extends the previous concepts to embrace the social structures and cultural patterns of groups and the practices of institutions. From these perspectives, power affects groups more than individuals (Gunn, 2006).

Since those perceptions are acquired based on historical development, and affect the interactions between the nature and objectives of control systems and systems of communication and power, the role of perception cannot be over generalised, because it is influenced by social, political and economic history that can be started by expanding it to include political cultures that consider the process of labour and structures of belief, as well as the history of society. Understanding social history is useful for understanding the expression of power, and how power relations between dominance and resistance occur (Gunn, 2006). Foucault indicates that knowledge is produced by 'discourse', which can be comprehended by exploring the institution producing the knowledge. Furthermore, Foucault suggests the notion of discipline, which has an important role in generating knowledge and power (Cowton and Dopson, 2002).

3.7. Discipline and Surveillance in Control Systems

In some areas, where power is established by a permanent structure it is perceived to circulate, and is not localised on a specific person. Therefore, an analysis should be undertaken on its effects, instead of its sources (Gunn, 2006). Power over and repression of individuals cannot be perceived solely in negative ways, but they also engender positive forces. For example, placing workers in a particular position is an embodiment of a power relation. Power in this understanding is not related to person or place, but to a relationship constituting an institution instead (Boland, 1987).

A historical approach can be employed to explore the exercise, practices, strategies, and technologies of power. In this sense, a state of power should be viewed as a set of practices rather than merely as an institution (Gunn, 2006). Hence, an administration should not be seen merely as the internalisation of rules and routines, but as the interrelation between order and discipline that consists of a set of practices embracing common-sense, experiences, and aspects of personal identity (McKinlay and Starkey, 1998). Activities that ensure the way subjected individuals or groups behave can be achieved through communication, and via the application of power such as through surveillance, reward, and punishment. These are enforced through a hierarchy, and their application might vary according to the different conditions in each organisation and how people perceive 'discipline' (Gunn, 2006). This notion implies that each region has different versions of truth dependent on its traditions and values. Hence, individuals are judged in accordance with these standards. This argument suggests that a version of truth came into existence and affected standards, virtues, and norms of society, a truth which is regarded as the intrinsic nature of reality (Macintosh, 2002).

Disciplinary power is efficient when it is imposed through administrative rules, and when it later raises resistance and legitimises disciplinary power (McKinlay and Starkey, 1998). Disciplinary power can be extended infinitely because it deals with the cognitive/emotional subject. In a knowledge/power relation, all of social science can be regarded as a discipline in two senses, i.e. as an intellectual discipline and as a discipline of repressive order (Boland, 1987). Based on the concept of knowledge/power, accounting is perceived as a set of practices and as a discourse to criticise, scrutinise, compare, and modify an organisation's member(s), which makes those members become knowledgeable, comparable to one another, and governable (McKinlay and Starkey, 1998). Norms form a field of discourse structured by normalising judgement and it is essential to make individual visible through a normative

judgement. Hence, individuals are constructed by a field of normative judgement (Boland, 1987). Power/knowledge is an effort to find the true nature of what is expected to be a 'normal' human being and use the knowledge to correct individuals in order to be in line with the 'normal' standard (Macintosh, 2002). Articulation of personal psychology is required for implementation of this concept. Therefore, the sophistication of accounting practices is required, as exemplified by the application of standard costing which is not only required for cost control, but also can be used to control the behaviour of organisational members (McKinlay and Starkey, 1998). Furthermore, McKinlay and Starkey (1998) perceive that this practice is a thorough surveillance instrument for managers.

Foucault, in his work *Discipline and Punish*, argues that prison, army, school, and workshop have the same structure, i.e. ways of knowing individuals (Boland, 1987). Foucault signifies that knowledge could become power to be used as a tool to discipline individuals who deviate from what knowledge perceives to be 'normal' (Macintosh, 2002). Disciplinary power embraces various ways of engaging with social life through the implementation of regulations and tools to manage the population and individuals' lives, whose identity is not perceived as comprising a homogenous sphere in wider society (Miller and O'Leary, 1987). For example, the mechanism of punishment in Europe in the 18th and 19th centuries used torture to acquire power, but later it was replaced by an impersonal surveillance system that relied on the psychology of the individual. The surveillance mechanism is exemplified by Jeremy Bentham's Panopticon, which is described as a prison in the shape of a circular building with a single observer at the centre able to see all the prisoners, although the prisoners cannot see the observer. Consequently, the principle of surveillance is internalised, and power functions automatically, without being exercised by external parties. In this sense, the Panopticon can be seen as an image of management control in general and accounting control in particular. Hence, accounting and management control both attempt to increase visibility in their particular fields. Through the application of responsible accounting, a manager is put in very special 'space' that can be monitored by the observer, as depicted in the Panopticon (Cowton and Dopson, 2002). Hence, accounting is not regarded as a neutral and objective tool, but as a picture of power relations that is brought into organisational and social life (Macintosh, 2002). For example, standard costing, accountability and responsibility are attached to each individual, which is intended to prevent inefficiencies at the individual level. Hence, the contribution of each individual can be identified, which requires constant

monitoring and observation. Through this method, the body and mind of individuals will be directed within the standard of economic performance (Miller and O'Leary, 1987).

In knowledge-intensive organisations that are identified as 'organic' rather than 'mechanistic', and in which creativity requires an absence of disciplinary power, cultural or normative control is developed as an alternative to bureaucratic control, which is perceived as a new technology of power. Normative control can be applied when particular practices and discourses are embraced by organisational members in daily life through an unspoken code, such as dress code, acceptable behaviour, etc. In this control mechanism there is a trade-off between self-subordination and personnel development (McKinlay and Starkey, 1998). Hence, there is a shift from formal techniques towards informal techniques, a shift which is regarded not as segregation, but as an element of governmental technologies (Lemke, 2007). Currently, surveillance by managers tends to be subtler than direct observation, employing such methods as written documents or records and information systems. The use of computers is useful to enhance surveillance over the operation of branches, particularly from a financial rather than a physical perspective. Surveillance will produce asymmetries of power which enable one group to rule over others (Cowton and Dopson, 2002).

Boland (1987) argues that Foucault's perspectives embracing the concept of disciplinary power, the relation between knowledge and power, the notion of visibility, and the process of normative judgement are closely related and hard to discuss separately. Exploring these ideas requires a specific institution along with a specific institutional problem, as Foucault notes (Boland, 1987). Macintosh (2002) argues that discipline and control can be realised by implementing three general principles, referring to Foucault's *Discipline & Punish*. The three general principles are the principle of enclosure, the principle of the efficient body, and the principle of the disciplined mind or comportment. The principle of enclosure can be employed by placing individuals in self-contained places of confinement. Putting an individual in this kind of place allows for the imposition of a monotonous disciplinary state. The self-contained place can be in the form of a horizontal or vertical partition that works hand in hand. The horizontal arrangement depicts a serial or functional chain, while the vertical arrangement can be defined as the hierarchical ranking of the partitions. In other words, the partitions also identify two states of function, i.e. the real and ideal state, in which the real state depicts the arrangement of a material object and the ideal

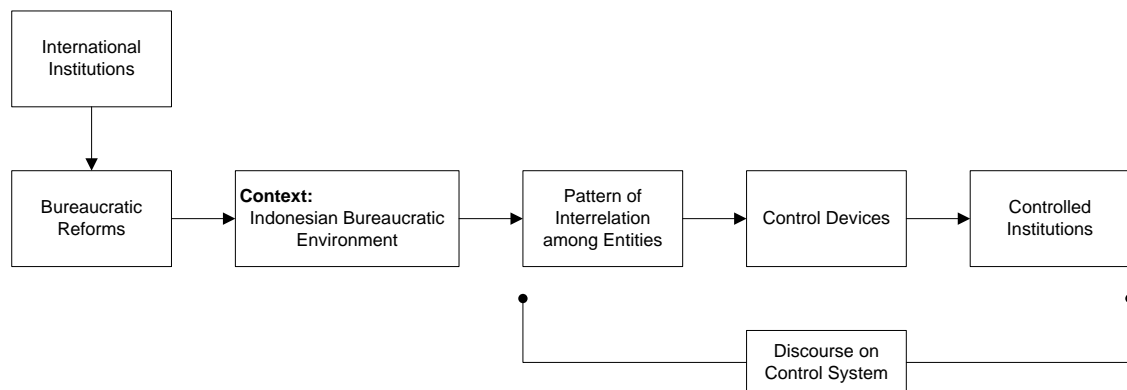
state describes the functions, serial relationships, and ranking of the partitions (Macintosh, 2002, p.84).

The second principle is regarded as a development of the previous principle, i.e. the efficient body principle, suggesting the efficient usage of time in any particular partition. The efficient body can be imposed in three ways: timetable, manoeuvre, and dressage. (i) The timetable approach is an attempt to ensure that time is used efficiently, and that any distractions are eliminated accordingly: "Time penetrated the worker's body, rendering it docile, obedient, and efficient" (Macintosh, 2002, p.84). (ii) The second approach is the manoeuvre: that is, techniques employed to intensify the usage of time by giving detailed directions and the exact timing of an accomplishment in order to link the individual body with a tool or machine (Macintosh, 2002). (iii) The third approach is dressage, which is perceived as a mechanism to "place the body in the world of signal" in order to initiate immediate responses and ensure obedience to do the particular action (Macintosh, 2002, p.85).

The final principle is the correct comportment or disciplined mind, which can be achieved through hierarchical surveillance, normalising sanctions, and examination. (i) The first mechanism is hierarchical surveillance, involving observation and the gathering of information, with the main functions of intensifying the constant surveillance of individuals' skill, punctuality, and commitment to their job. (ii) The second mechanism of a disciplined mind comprises the normalising sanctions that are applied by giving rewards and punishments. The sanction is intended to motivate individuals to achieve the higher level of competence instead of inducing individuals to adhere to the established norms of correct behaviour. Use of this sanction is to be avoided if possible, it suggested, referring to the assumption that a deviant individual can be motivated more by the desire to acquire promised rewards than by the fear of being punished by sanctions. "The positive use of sanctions was much preferred" (Macintosh, 1994, p.226). Employing sanction mechanisms at work both automatically and silently will induce individuals to correct themselves, adhere to the norm, and be motivated to improve – "Quiet sanctioning produced normalisation" (Macintosh, 2002, pp.87-88). (iii) The third mechanism is examination, which suggests that the result of examination can be used as a justification for sanctions, and the combination of these two mechanisms are regarded as an integral part of the principle of a disciplined mind. Examination can be used as a mechanism to reveal the special attributes, characteristics, and capabilities of individuals, which becomes knowledge held by one party. This

acquired knowledge can then become a power held over other parties. Hence, “the individual existed as a thing to be corrected, normalised, and treated in accordance with the discursive practices of that particular discipline” (Macintosh, 2002, p.89). From this view, the individual is self-normalised based on the discursive regime of truth rather than on “any final true existence” (Macintosh, 2002, p.115). The discourses of power, knowledge, surveillance, and discipline in the control system in particular are depicted in Figure 3.1.

Figure 3.1. Conceptual Framework



3.8. Research Method and Design

The quantitative and qualitative approaches in social research are regarded as complementing each other, although in some aspects these approaches are very different (Creswell, 2003). The differences are particularly evident in the ways in which these studies collect and analyse data in order to understand patterns. Another difference between the two research approaches is in the nature of the data employed. Qualitative research relies more on the interpretation of *soft data*, which can be observed in impressions, words, symbols, and photographs. Hence, the qualitative researcher must consider the ‘case and context’ of the data (Neuman, 2007), which enables such a researcher to investigate social phenomena holistically (Creswell, 2003). Meanwhile, quantitative research employs ‘hard’ data in the form of numbers; an approach that focuses on ‘measuring variables and testing hypotheses’ (Neuman, 2007).

Referring to these characteristics, this study employs a qualitative approach, because the research relies heavily on soft data, which are affected by cultural and historical contexts, in order to comprehend practice control mechanisms operating in Indonesian local government. Moreover, the qualitative approach is deemed to fit well with this study, which is expected to provide detailed descriptions concerning an

analysis of human experience (Marvasti, 2004), with a particular focus on managing the control of capital expenditure in relation to other parties. Hence, this study explores how power relations in local government organisation, which are influenced by cultural and historical backgrounds, affect the strength and efficacy of the control mechanisms of capital expenditure in Indonesian local governments.

The qualitative approach in this study also requires an analytical method for analysing the acquired data, specifically *discourse analysis*. Discourse analysis considers the interrelationship between language and power because language can be perceived in terms of social practices (Wodak, 2001). The aim of this method is to investigate social conditions and processes that are expressed, signalled or legitimised by language (Wodak, 2001). In addition, discourse analysis is also regarded as an effort to conceptualise discourse as a social phenomenon, and then to find explanations for it, determine how it happened and investigate the structure of the phenomenon. Therefore, Teun van Dijk (as cited in Wodak 2001, p.20) defines it as “a framework systematising ‘phenomena of social reality’ and a ‘communicative event’”. As indicated by Fairclough: “every social practice has a semiotic element”(Meyer, 2001; Fairclough, 2001). Therefore, this method covers three social concepts: the concept of power, the concept of history, and the concept of ideology (Wodak, 2001).

In this study, the discourse analysis is employed to capture social phenomena that are applied by influential parties to local government and to identify social phenomena in the internal of particular local government. Referring to the identified social phenomena, then it will be analysed based on how do the phenomena emerge in particular relationship based on historical and cultural view; how does ideology affect the relationship; and how can the phenomena be used as a ‘power’ by one party to another party. Furthermore, this study also identifies how strong the phenomena affect practices in particular local government; and how do the local government deal with it. Hence, this study embraces many discourses related capital expenditure control system along with the influence of formal control to the social phenomena at local government level.

3.9. Case Study

A case study is a methodological approach to gathering information about a particular social setting, event, person, or group in order to comprehend how the particular condition/situation works (Berg, 2001). Sometimes, the term ‘case study’ is

interchangeable with qualitative research and even treated as a synonym, because much qualitative research is in the form of a case study (Bryman, 1989). Furthermore, Bryman (1989, p.143) suggests that the nature of a case study embraces several aspects. First, the definition of 'case' is broad: it can be an organisation, department, person, or event. Second, the case-study approach does not necessarily involve one case on one site, but it can be related to two or more sites, meaning that it can enhance the generalisation output of the research. However, the aim of the case-study approach is to develop patterns and linkages on a theoretical basis, instead of inferring findings from a population. Third, this study focuses on context, an approach that should make a reader feel engaged in the particular organisation being studied, as well as provides insights that can help to interpret events. This approach is very useful for examining the impact of a policy, because it can depict the implementation of that policy in day-to-day activities.

Particularly in the UK, the case-study approach is applied by referring to the work of social theorists such as Habermas, Foucault, and Giddens (Scapens, 1990). Furthermore, Scapens (1990) suggests that in the accounting management area the case-study model could provide insights into the nature of management of accounting practices in relation to techniques, procedures, and systems. These management accounting components can be studied by distinguishing the formal systems that are supposed to be implemented from the ways the systems are actually used. Case studies can be applied in various ways. First, a descriptive case study can depict an implementation of accounting systems, techniques and procedures. Second, an illustrative case study will demonstrate innovative practices developed by companies. Third, an experimental case study is intended to examine the implementation of a new system and evaluate the advantages and disadvantages of that system. Fourth, the exploratory case study tries to find reasons for particular accounting practices, and attempts to generate ideas that will be examined by empirical testing to produce generalisations of those practices. Finally, there is the explanatory case study, which is designed to explain particular reasons for the implementation of certain accounting practices. Theoretically, the case-study method is used in order to provide a framework to comprehend and explain specific practices, instead of producing generalisations (Scapens, 1990, p.265). This case study fits with the fourth aim, and is intended to explore mechanisms of control of capital expenditure that can be used as a starting point for future studies in this area.

A case study in management accounting refers to social theory because accounting practices are socially constructed (Scapens, 1990). Hence, the researcher tries to find out the structure of social behaviour that constructs and informs practices. In order to study management accounting as social practice, it is suggested the researcher should probe the relationships between social action and the dimensions of social structure in an organisation by considering the historical, economic, organisational, and wider social context as well. Understanding the complex inter-relationships of many components in a system is required in an attempt to construct explanatory social theories (Scapens, 1990, pp.268-269). Referring to all of these characteristics, this study is best-suited to employing the case-study approach, because the research focuses on organisational sociology in Indonesian local government. Hence, local government organisation cannot be separated from the many elements of the public, from central government, and also from political aspects. Therefore, inter-relationships among parties affecting local government, particularly in capital expenditure decisions, will be explored by considering their organisational and cultural contexts, which is expected to provide an understanding of how those organisational and sociological aspects affect capital expenditure control.

3.10. Qualitative Research

As mentioned in the previous sections, this study employs the case-study approach to acquiring data, and discourse analysis to analysing data. With regard to the case-study model, there are several stages to undertaking this type of study, as suggested by Scapen (1990). However, the stages do not simply follow a linear order, because a case study is regarded as a complex interactive process; hence, a different order and different interactions between the stages are likely to occur (Scapens, 1990). The stages start with the preparation stage. After the researcher finds a case, it is suggested to review the available theories that are relevant to the case from the researcher's point of view. The applied theory should be stated explicitly and comprehensively. The second stage is collecting evidence. The preferred theory gives an indication of the types of evidence that need to be collected. The evidence can be collected formally in several ways, such as interviews, documents, direct observation, or participant observation. However, the researcher must also be aware of the possibility of gathering informal evidence, such as comments, or information in the form of the tone of an answer, facial expressions, and gestures or body language. Such informal

evidence can be useful for developing predetermined questions in order to explore several issues, and for providing an indication concerning the validity of the formal evidence.

The third step in the case study's progress is assessing the evidence. In a quantitative study, reliability and validity of evidence are essential; reliability is regarded as the independence of the evidence from the researcher, which means that the evidence must not have any relationship with the researcher. Meanwhile, validity corresponds to the perception that the acquired data are 'true', or have an objective and accurate reality. However, the reliability and validity approaches described above do not fit with a case study, where evidence comes not only from formal sources but also from informal sources, such as 'external' factors, which help in the interpretation of formal evidence. Hence, validity in a case study can be assessed by particular conditions, known as 'contextual validity'. Contextual validity can be examined in several ways. *First*, the validity of evidence can be assessed by other kinds of evidence concerning a particular issue, an approach that is also known as triangulation. *Second*, the validity of evidence acquired from a particular source can be assessed by other evidence collected from the same source. If any inconsistency emerges from the source, the researcher can determine the validity of the evidence. *Third*, validity can also be assessed by other members of the research team, in order to eliminate bias that might arise from the personal characteristics or experiences of a researcher. *Fourth*, feedback from subjects of study is also useful to confirm the researcher's interpretations of the data. This study employs the first approach, which assesses particular issues from other sources, i.e. transcripts of interviews of secondary sources, and documents in the form of laws and regulations related to the issues.

The fourth stage is identifying and explaining patterns. After all the evidence has been collected, the researcher needs to identify themes and patterns emerging from that evidence. In order to understand connections between the themes, preparing a model is suggested. Subsequently, the patterns indicated in the model, which may be related to prior studies and/or an underlying theory, can be used to describe and explain the case. Meanwhile, any inconsistencies or missing connections within the pattern can be used as bases for further study. The fifth stage is theory development. In case the pattern is inconsistent with the existing theory, it is necessary to collect evidence in an attempt to explain this difference. In such a situation, a theory can be developed to approach and explain the new findings. However, the researcher is also required to set

the boundaries of his/her study, because essentially the pattern of the case-study model can be extended indefinitely. The final stage is report writing, which is intended to make the case and explain the context in a way that can be comprehended by other parties. In addition, the report is also useful to describe theoretical implications that might affect other studies (Scapens, 1990).

Discourse analysis is employed in this study, because it studies discourse as text and discussion in social practices, and hence focuses on what people do. There are several important points about this model that need to be noted. Since discourse analysis looks at products of human action, the conception of that action affects the main features of discourse, i.e. action orientation, situation, and construction. The first feature is action orientation, where discourse is perceived to be the primary medium of human action and interaction, which can be characterised either in a general or specific setting. The second feature is the situation, which perceives discourse to be situated in one of three contexts: sequential, institutional, and rhetorical. In general, the rhetorical context is defined as a version of event or action used to counter alternatives, and therefore requires an understanding of the sequence of a particular event or action (Potter, 2004). Finally, the third feature is construction, i.e. where discourse is both constructed and constructive. Discourse is *constructed* because it is developed from various sources, and *constructive* because it can be used to build and stabilise particular versions of events or actions (Potter, 2003). Furthermore, referring to those features, Potter (2003) suggests how to do an interview involving discourse analysis. *The first suggestion* is the focus, which concentrates the interviewer on predetermined themes and direct questions to provoke participants to elaborate on discursive issues. *The second suggestion* is standardisation, which ensures all participants have the same perception about the themes (Potter, 2003). Referring to Potter's (2003) suggestion, this study pushes the primary sources to elaborate more on particular discourses.

3.11. Method of Data Collection

Indonesia is the largest archipelago country in the world, comprising 530 local governments consisting of 497 municipalities, and 33 provinces (Depdagri, 2010) that are spread throughout 17,508 islands (Indonesia, 2012). In October 2012, the Indonesian Parliament approved the 34th province. It is impossible for this study to cover all areas, because the nation of Indonesia is too huge. Therefore, this study adopts a case-study model for one province: the special region of Yogyakarta. This province

consists of a city and four districts: Yogyakarta city, and the four districts of Sleman, Bantul, Gunungkidul, and KulonProgo. This province was chosen because it is located in the centre of Java Island. Hence, it can be said to represent the typical conditions of other regions in Java Island, apart from Jakarta, Indonesia's capital city, which is also located in Java Island. Moreover, the special region of Yogyakarta has a long history of governance and culture that differentiates it from the other regions in Java. Thus, it can be employed to explore the influence of cultural and historical aspects on current practices.

Local government agencies were selected based on total capital expenditure, compared to other agencies. In each region, 10 agencies were selected, plus the inspectorate as an internal auditor in each region, one of the main responsibilities being to ensure the implementation of internal controls in each agency. Finally, 66 local government agencies were selected to be the targets of the research interviews. However, only 38 local government agencies were willing to be interviewed to provide samples for this study. The study obtained 38 interview recordings, but of these, one interview's results were excluded because the recording could not be clearly heard and the answers did not focus on the questions. As a result, only 37 transcripts are employed as data for this study. The interview participants were 67 local government officials in various positions, from a head of a local government agency to planning and/or financing officials as listed in appendix 7. The main targets of the interviews were local government officials engaged in planning, financing, and accounting activities. Head and/or middle management officers were selected because officers at this level have knowledge of and understand the reasoning behind the policies and practices in each organisational unit. In terms of implementation of local government programmes, they must refer and adhere to many regulations both from central and local government before implementing those programmes. Concerning confidentiality, the interviewees are not mentioned by name but in the form of a code of their position instead, and their name will not be revealed to the public. Even, some comments that are regarded to be sensitive will be kept anonymous.

The primary data were collected via semi-structured interviews consisting of seven main questions, as set out in appendix 8, but the questions were then developed following the participants' answers. All of these interview questions were open-ended, embracing several aspects of capital expenditure, including sources of capital expenditure funding, considerations for accepting a capital expenditure proposal,

obstacles that might arise from interactions with other parties in accordance with the current procedures, and efforts made by government officials to deal with those issues. This interview method was employed in order to explore in-depth aspects of capital expenditure, and was further developed based on the conditions pertaining in each agency. The interviews were recorded and transcribed into the Indonesian language. Additional translation into English was undertaken when quotations and examples of statements were required.

Secondary data are also used in the study, acquired from the website: www.princeton.edu/successfulsocieties. This website contains interviews with Indonesian notables from many backgrounds, such as economists, politicians, ministers, and government officers, which took place between 2009-2012 (see appendix 9). The data from this website comprise recordings and transcripts of the recordings. This material was employed after permission was obtained from the administrator of the website. This study uses 12 transcriptions for data analysis, which are important descriptions of the perceptions of the central government officers or persons who have a direct connection to the central government decision-makers relating to decentralisation and the new management controls which came along with the decentralisation policy. The archived descriptions give context and background to this study.

Finally, including both primary and secondary data there are 49 samples/cases that have been subjected to discourse analysis. At the first stage, based on transcriptions of the interviews, the researcher has identified themes that emerged from each transcript. In order to enable the identification of themes, the researcher employed the NVIVO software. This study not only considers dominant themes but also non-dominant themes. Therefore, other aspects that cannot be categorised into a particular code are sorted into the 'other' category. As a result, the total number of transcripts codes is 210. Subsequently, the codes were re-assessed and re-grouped based on some commonalities in order to develop categories or themes. After the re-assessment, the codes were classified into 22 themes. Then, all the themes were placed into a framework showing how many parties who have an interest in capital expenditure interrelate.

3.12. Summary

The main purpose of this chapter is to explain the analytical basis of the case study. It employs Foucauldian perspectives, particularly of power, knowledge,

surveillance, and discipline, on establishing control. Control is perceived as a power to direct organisational members to adhere to all regulations that have been established. Although the application of power potentially provokes resistance from the subjugated individual, domination through power needs to be maintained in many ways, such as through knowledge, surveillance, and disciplinary power. An organisation can be seen as a coalition of individuals that are highly susceptible to conflict. In this circumstance, control systems are required to identify the commitment and expectations of individuals as members of the 'coalition', a process which requires individuals to be observed, measured, and supervised. From this perspective, accounting is regarded as a social and organisational practice (Miller and O'Leary, 1987).

In addition, this chapter is intended to show how the best research approach was chosen to fit with the proposed conceptual framework for this study. This study employs qualitative research because it is intended to explore current practices of control mechanisms in Indonesian local government, especially in capital expenditure. The case-study model is employed in this study in order to enable in-depth exploration regarding the particular case, by investigating the perspectives offered by a sample of local-government officials. The primary data of this study were gathered through semi-structured interviews, which enabled the researcher to develop questions that could elicit more information regarding particular issues. The interviews were conducted in the offices of each local government agency so that informal information could be added to the formal information collected at the same time. The informal information is expected to give insight into the working environment of the sampled local government agencies.

Since the subject of this study is public institutions, which tend to be very sensitive on the issue of government laws and regulations, it focuses on those laws and regulations that have been implemented by Indonesian local government. This is intended to support the acquired primary data. The secondary data from the archival interviews with notable figures in Indonesia's government, who were involved in decision-making about the nation's bureaucratic reforms, and thus could give insights into such a major change process, supplement the primary data.

The next chapter elaborates on the findings of this study, with emphasis on the implementation of control in capital expenditure, particularly in relation to 'external

actors', their decision-making, and their interactions, and how these interrelationships might strengthen/weaken the control of capital expenditure.

Chapter 4

External Parties Affecting Capital Expenditure

4.1. Introduction

The previous chapters have discussed the context of this study and the research methods employed in this study. Chapter 2 discusses the context of this study, which begins with the agendas of international institutions and the impact of those agendas, particularly on Indonesian local governments. Chapter 3 addresses the conceptual framework of this study, along with the methods employed in conducting this research, by referring to the context of this study. Now, Chapter 4 will depict the empirical findings, which have been obtained by employing the research methods described in Chapter 3. This chapter identifies parties affecting local government, particularly

external parties associated with local governments who influence capital expenditure in some way, both directly and indirectly. There are many organisations or institutions involved in capital expenditure decision-making, which include both formal and informal bodies, such as BPK, BPKP, LKPP, NGO, local society, etc. It has been suggested by international institutions in the Letter of Intent (LoI) that the involvement of these organisations/institutions needs to be established or empowered in order to enhance the transparency and accountability of public expenditure.

The main aim of this chapter is to elaborate on the issue of the financial control mechanism that has been determined by the central government of Indonesia. In the first place, an extensive study on the legal basis for the interrelationships between many parties and local government is carried out. From the study, it can be identified three parties affecting control mechanisms on capital expenditure; these are regulators, oversight bodies and stakeholders. Subsequently, this chapter identifies the influential external parties in real practice from the point of view local government officials; how are they interrelated, how do they affect capital expenditure decisions, and how their involvement in capital expenditure decision-making might strengthen or weaken capital expenditure control. Also, this chapter investigates how those agencies deal with the engagement of the external parties.

This chapter is structured as follows: the first section addresses the initial control of public expenditure, which is undertaken through budget setting and the empowering of auditor agencies, along with establishing government accounting standards as a guideline for conducting audit assignments. The second section describes fixed assets and methods of acquiring those assets, along with acquisition costs that must be considered in order not to exceed the budget. The third section looks at the involvement of external parties in the capital expenditure decision that include budgeting or the implementation of the budgeting stages. The fourth section depicts influence of the external parties on control mechanisms of capital expenditure in local government agencies. The final section is a summary of the chapter.

4.2. Budgeting as the First Stage of the Control Mechanism of Public Expenditure

The financial system of Indonesia's local government begins with the composing of a budget for each local government agency. Then, the budgets of all agencies are compiled at the local government level to become the local government's

budget. The influence of political processes in budgeting decisions is immense, particularly when the executives compose a budget and submit it to the legislative body to get approval. Later, after the budget is approved, the executive holds full responsibility for the implementation of the financial aspects to the legislature and society, based on current regulations (PSAP, App.2, par.9). Basically, the government's budget is a formal document based on the agreement between executive and legislative bodies regarding government spending and revenue generation. The budget is regarded as a tool of coordination between spending activities and the availability of funding in a certain period.

Moreover, the budget plays an important role in several ways: the budget is regarded as a public policy statement; it is a fiscal target; it is the basis of control along with legal consequences; it is a basis of performance assessment; and details of the implementation of the budget will be contained in accountability statements from the government. Hence, the interrelationship between accounting and financial statements relating to the budget is very close, because the budget is the starting point of implementation programmes that are later expressed in the financial statements (PSAP, App.2, Par.13). The term *government* in this regulation refers to the central government and to local government, which have separate accountability and authority towards particular assets, jurisdictions, tasks and missions (PSAP, App.2, Par. 19-20).

Within Indonesian local government, public expenditure is highly regulated in order to protect the utilisation of public funds. Therefore, the Indonesian government has issued several regulations intended to strengthen control of public expenditure. For example, a government regulation (PP 24/2005) regarding government accounting standards was issued, in which the government accounting standards committee referred to several professional bodies. These professional bodies consisted of the International Federation of Accountants, International Accounting Standards Committee, International Monetary Fund, Indonesian Institute of Accountants, Financial Accounting Standards Board, Governmental Accounting Standards Board, and other professional organisations from other countries, all of which regulate financial statements, government accounting and auditing (PSAP, App. 1, par.13.). The issuance of the government accounting standards can be regarded as a milestone of bureaucratic reform when compared to the absence of accounting standards in the previous era. Accounting standards are required as guidelines with which to prepare financial statements in accordance with the principles of transparency and accountability,

particularly for public expenditures informing the implementation of local government budgets. In addition, the government accounting standards committee also considered the internal environment of the Indonesian government. In particular, the committee addressed the characteristics of government structures alongside the services provided, embracing the form of government and segregation of power, an autonomous governmental system and financial transfers between governmental levels, the influence of political processes, and the interrelationship between taxes and government services (PSAP, App.2, par.7).

4.3. Mechanism of Capital Expenditure

Based on government accounting standards, assets, in general, are defined as economic resources possessed by a government as a result of past transactions which have economic benefits that can be measured by financial instruments. Meanwhile, fixed assets are defined as tangible assets that have an economic life of more than 12 months. Economic life is specified as the period of time for which assets are to be employed by the government or the public; or the total production expected to be acquired from government activities or public services. The value of the fixed asset is measured by cost, which is determined as cash or a cash equivalent paid to acquire an asset until the asset can be utilised. Considering the utilisation of the asset also involves taking into account the depreciation, carrying amount and residual value of the asset. If the asset is to be exchanged with another asset, it will be considered to be the fair value of that asset (PSAP 07, par.5).

Acquiring costs for equipment consist of the total expenditure incurred, starting with the cost of the equipment, transportation, installation, and other direct costs until the equipment can be utilised. Meanwhile, acquiring costs related to building and construction tend to be more complicated, because they involve more cost components, such as completion or acquisition costs, construction permits, tax, and notaries' fees. Meanwhile, common costs and administration costs, which cannot be attributed to a particular asset, cannot be regarded as acquired costs (PSAP 07, par.32). The other type of fixed asset is an infrastructure asset, which has several features: it is part of a system or network; it has a specific characteristic and cannot be converted to another function; it cannot be moved to another place, and there are restrictions on disposal of the asset. Some examples of infrastructure assets are roads, bridges, sewage systems and communication networks (PSAP 07, Par.72).

Before construction of the assets is undertaken, the government is required to set a construction contract as a specific agreement for the construction of an asset or combination of assets that are closely related to each other with regard to design, technology, and the main functions of the asset(s). The contract is set by the government to inform the contractor undertaking the project. The term *contractor* can be applied both to entities that build an asset and to entities providing construction services based on specifications that have been established in the construction contract. After the contract has been signed by the contractor, as chosen via the procurement process, the project can be started. Prior to that moment, the government must make a down-payment based on the payment terms that were agreed in the construction contract. As the payment has not yet been paid in full, the contractor is still owed remaining payments, which will be made when all the conditions determined in the contract have been fulfilled; this is known as retention (PSAP 08, Par.5). However, construction contracts should include several categories of work that started with the planning of an asset; these are the contract for services of asset construction, such as structural design services, the contract for the construction of the asset, the contract for the supervision of construction work and evaluation, and the contract for the disposal or restoration of the asset and the environment (PSAP 08, par.9).

4.4. Many Parties affecting the Capital Expenditure

A flowchart of capital expenditure is depicted in appendix 10, which describes the interrelationships of many government institutions in determining local government budgets, including budgets for capital expenditure. The figure portrays several parties, including the Ministry of Internal Affairs, governors, local governments, local government agencies and local parliaments. However, other parties might also be involved in the implementation stage of the budget, as suggested in appendix 10.

4.4.1. Interrelationship with the Ministry of Home Affairs (MoHA)

The MoHA, as the main regulator of local governments, plays some very important roles, beginning with producing regulations related to issues such as decentralisation, fiscal balance, and governance of local governments. The MoHA has produced guidelines on the utilisation, supervision, monitoring, and evaluation of fiscal balance between central government and local governments (UU 32/2004 art.163). Meanwhile, in terms of establishing good governance, particularly relating to the

budgeting process portrayed in appendix 10, the MoHA plays different roles: at the first stage it sets guidelines for the formulation of local budgets that are used as a reference for local governments to compose a draft of general policy for the local budget (KUA / *Kebijakan Umum Anggaran*). KUA is a document which consists of general policies on incomes, expenses, and funding, along with predictions for the fiscal year (Permendagri 13/2006). The guidelines of KUA contain several points relating to local budgets: the first concerns key issues regarding the synchronisation policies of local governments with the central government. The second point concerns the principles and policies composing the local budget, such as determining the performance measurement of local government programmes. The third point relates to technical issues involved in composing the local budget, such as forecasting local government income, allocation of local government expenditures, sources and uses of funding, along with underlying assumptions. The final point relates to the specific issues of a local government (Permendagri 13/2006 art. 83-84).

The second role of the MoHA in determining the local budgets of local governments, as depicted in appendix 10, is to authorise drafts of local ordinances concerning the implementation of local budgets. Thereafter, drafts of local ordinances become actual local ordinances, ready to be implemented. The local ordinance must contain the following main points of the local budget: a summary of the local budget; local budget breakdown by agency, programmes, objectives, funding and expenses; the number of government officials; local government investments; a forecast of fixed assets and other assets; unfinished programmes from prior fiscal budgets; a reserve fund; and local government debt (Permendagri 13/2006, art. 107).

4.4.2. Interrelation with Local Parliament

Besides interacting with the MoHA regarding decisions relating to local budgets, the local government is required to interact with the local parliament as a counterpart of the government in its legislative function, and as the representative of local society. Based on regulations, the local parliament (DPRD / *Dewan Perwakilan Rakyat Daerah*) has an obligation to improve democratisation in the governance and welfare of local society. This obligation reflects democratic participation, which facilitate local society to communicate their aspirations and complaints. Then, these inputs need to be followed up by the local parliament (UU 22/1999 art. 22). Hence, the parliament has a right to refuse or accept the accountability reports of the heads of local

governments, particularly related to the management and achievement of public finances in terms of efficiency and effectiveness in the implementation of decentralisation (UU 25/1999 art.24). The local parliament comprises members of different political parties. The head and vice-head of local government are also supported by particular political parties, as are at least 15% of the members of local parliament; the process of acceptance or refusal of the accountability report is therefore influenced by the political constellations.

The local parliament is involved in the budgeting process in three ways (see appendix 10). First, the local parliament, together with the head of local government, discusses a draft of the general policy for the local budget (KUA / *Kebijakan Umum Anggaran*); as a result of this communication, the draft will be ratified. Second, the local government agency composes a draft of priorities and a temporary budget ceiling (PPAS / *Prioritas dan Plafon Anggaran Sementara*). The PPAS presents the priority of programmes and budget ceilings for every local government agency programme, and will be used as a reference with which to compose the work plans of those local government agencies (RKA-SKPD / *Rencana Kerja Anggaran – Satuan Kerja Perangkat Daerah*) (LKPP, 2012). A draft of PPAS is based on the following stages: (1) determine a priority scale between obligatory and optional functions; (2) determine a sequence of the selected programmes; and (3) determine a temporary budget ceiling for each programme. Then, the head of local government compiles the PPAS and discusses it with the local parliament. The discussion is led by the budgetary team of the local government (TAPD / *Tim Anggaran Pemerintah Daerah*), as representatives of the head of local government, and the budget committee of local parliament. After the draft of the PPAS is approved, it will become the priority and the budget ceiling (PPA / *Prioritas dan Plafon Anggaran*) that will be employed by each local government agency. Officially, before it is employed, the ratified KUA and PPA will be signed by the head of local government and the head of local parliament in a MoU (Permendagri 13/2006, art. 87-88). Therefore, the local parliament is also responsible for supervising the implementation of the local budget (Kepmendagri 29/2002 art.96), a procedure which is known as legislative supervisory (PP 20/2001 art.1).

Finally, the third form of local parliament involvement is in the process of issuing local ordinance about the local budget. The head of local government submits a draft of local ordinance about the local budget, by the first week of October at the latest, which must be ratified at least a month before the fiscal year begins. If the deadline

cannot be met by the local parliament, the local government might apply the same budget ceiling as the previous year, particularly for obligatory expenses, such as personnel expenses and goods and services expenses, which continuously need to be met in order for local government to fulfil its basic public services (Permendagri 13/2006, art. 104-106).

4.4.3. Interrelation of the Local Government with other Ministries

In addition to the relationship with the MoHA, each local government agency is closely related to other technical ministries that supervise the technical agencies; for example, the agriculture agency will carry out programmes and will be supervised by the Ministry of Agriculture. The related ministry must compile reports on all projects and categorise the reports based on sectors and sub-sectors of capital expenditure, organisational units for routine expenditure, and distinguish which projects are managed by central government and local government (UU 25/1999 art.31).

The Ministry of Finance (MoF) also plays important roles, especially relating to regulating financial aspects of local government, such as the implementation of local government financial information systems (UU 25/1999 art.27). The MoF issues its own decree to regulate local government finance, such as PMK 183/2014, which regulates the limits of local budget deficits, PMK 06/2012 concerning the implementation and accountability of budget transfer to local governments, and several ministerial decrees (PMK 216/2010, PMK 209/2011 and PMK 180/2013) regarding specifically allocated funds (DAK / *Dana Alokasi Khusus*). In addition, the MoF also issued PMK 238/2011 in order to endorse the implementation of government accounting standards.

Meanwhile, the Ministry of State Apparatuses and Bureaucratic Reforms has an important role in regulating all aspects of government officials, both in central and local government. For example, the ministerial decree (Permenpan 09/2009) regulates implementation, supervision, evaluation and reporting as a follow-up of the functional audit that was conducted by the BPK as the external auditor. The APIP (*Aparat Pengawas Internal Pemerintah* / government apparatuses of the internal auditor) consists of the BPKP, the inspectorate general for ministries, and the inspectorate of provinces, cities and districts. The APIP has to adhere to the guidelines of audit quality control that have been asserted in Permenpan 19/2009. The head of an agency is responsible for the implementation of programmes that will later be assessed to

determine the performance of the institution. Good performance by government institutions is also rewarded by increasing the salaries of government officials; thus, the ministries decided to give remuneration to all government officials by issuing Permenpan 08/2009.

4.4.4. Interrelation Local Government with Oversight Bodies

The main oversight body in the Indonesian government is the BPK (*Badan Pemeriksa Keuangan*), Indonesia's supreme auditor which is responsible for auditing the management and accountability of public finance (UU 15/2006 art.1). The scope of the audit the BPK covers is broad; it covers financial audit, performance audit, and audit for a special purpose, which addresses all government institutions using public finances, including central government, local government, and publicly owned companies. However, this responsibility can be delegated to public accountants, who are held responsible to the BPK and who must submit audit reports in order to be published by the BPK (UU 15/2006 art.3).

In order to do audit assignments, the BPK refers to government regulations and guidance that have been disseminated to local government as a starting point (UU 32/2004 art.221). Dissemination and tutoring regarding the management of local government finance are the responsibility of the MoHA, but the governor at a provincial level might also give training to municipalities as long as such an initiative does not contradict the MoHA guidance (Kepmendagri 29/2002 art.94-95). In addition, in conducting an audit the BPK also refers to general standards of financial statement, standards of auditing, and standards of reporting (UU 15/2004 art.1). As required in an audit, the BPK must perform analysis and assessment of the internal control system of local government (UU 15/2004 art.12). Additional information can be gathered from the audit reports of internal auditors, because the internal auditor (BPKP / *Badan Pengawasan Keuangan dan Pembangunan*) is required to submit its report to the BPK. Moreover, information can also be obtained from independent institutions, such as the KPK (*Komisi Pemberantasan Korupsi* / Commission of Corruption Eradication), the KPPU (*Komisi Pengawasan Persaingan Usaha* / Commission of Supervision of Business Competition), and the PPATK (*Pusat Pelaporan dan Analisis Transaksi Keuangan* / Centre of Reporting and Analysis of Financial Transactions), as well as from professional associations and public complaints. In an audit assignment, the BPK is allowed to employ experts from outside to work on its behalf (UU 15/2004 art.9).

The role of the BPK as an auditor is the implementation of functional supervision, as suggested in PP20/2001 art.1.

Regarding audit reports, the BPK must submit the audit report to local parliaments and to the heads of local governments (UU 15/2004 art.17; UU 15/2006 art.6). The BPK also gives opinions on the audit report in the form of professional statements about the fairness of information in the financial statements of the local government, which refer to four criteria. The first criterion is compliance with government accounting standards; second, adequate disclosure; third, conforming to government regulations; the last, effectiveness of internal control systems. The BPK might give one of the following opinions: an unqualified opinion, a qualified opinion, an adverse opinion, or disclaimer of opinion (UU 15/2004 art.16).

Therefore, the BPK has an important role to play in establishing government accounting standards (SAP / *Standar Akuntansi Pemerintahan*). After obtaining feedback from the BPK, the draft is legalised as the government accounting standard (PP 24/2005). The SAP enshrines the principles of government, both central and local, as an accounting entity to prepare and present financial statements. Moreover, in order to ensure the reliability of the financial statements, the central government needs to establish an internal control system as an integral process involving all organisation members. This system is also needed in order to secure government assets, compliance with regulations and, finally, to ensure the achievement of organisation objectives (Permenkeu 233 PMK.05-2007).

Apart from the BPK having a role as external auditor, the GoI also has the BPKP (*Badan Pengawas Keuangan dan Pembangunan* / Supervisory Agency of Finance and Development) as the internal auditor of the GoI, which was stressed specifically by presidential decree (Keppres 31/1983) in the pre-reformation era. The BPKP's main responsibilities can be broken down into two categories: (1) supervision of acquiring and managing of finance, and (2) supervision of development programmes (Keppres 31/1983 art.2). These responsibilities encompass compliance with regulations, and assessment of the effectiveness and efficiency of the usage of government facilities, in an attempt to achieve determined programmes (Keppres 31/1983 art.40). In order to accomplish this, the BPKP must carry out several tasks, both at central and local government levels, such as assistance, counselling, and monitoring of all supervisory

apparatus; conduct control regarding income and expenses, fixed assets and state-owned enterprises; control and evaluation of administration systems (Keppres 31/1983 art.3).

In the post-reformation era, the position of the BPKP in Keppres 31/1983 has been strengthened by presidential decree (Keppres 103/2001), and the latest attempt to strengthen the BPKP was Perpres 192/2014. Perpres 192/2014 places more emphasis on the role of the BPKP as the internal auditor than did the previous presidential decree. The role and performance of the BPKP are now directly under the supervision of the nation's president (Perpres 192/2014 art.1). As under previous presidential decrees, the BPKP focused on the accountability of financial management and is related to cross-sectoral programmes (Perpres 192/2014 art.18-19). In Perpres 192/2014, this responsibility is extended to include establishing the government's internal control system (Perpres 192/2014 art.38).

In addition to the two existing oversight bodies, the GoI established several new oversight bodies during the reformation era. One of the new overseeing bodies is the KPPU (*Komisi Pengawas Persaingan Usaha*, or Commission of Business Competition Supervision), an independent institution free from any interventions from the government or any other parties, a status assured by UU 5/1999 and Keppres 75/1999. However, the KPPU is funded from the national budget (APBN / *Anggaran Pendapatan dan Belanja Negara*) (UU 5/1999 art.37). This commission is appointed and dismissed by the country's president, with approval from parliament; the tenure of the commission is five years. The commission and its members are directly responsible to the president (UU 5/1999 art.30-31), and hence the KPPU must provide reports to both the president and parliament on a regular basis (UU 5/1999 art.35). The main responsibilities of the KPPU are to assess any practices resulting in or from unfair business competition, to identify any monopolies, and to compose guidelines relating to the prevention of such practices. The KPPU has the authority to take any necessary action to counter these practices and to give input to the government relating to unfair business competition and monopolies (UU 5/1999 art.35). This attempt to establish and maintain a level playing field is intended to ensure a business climate conducive to the success of small, medium, and large enterprises (UU 5/1999 art.3).

The KPPU can acquire information about unfair business competition from many sources, such as from the public or the business community. Based on such information, the KPPU conducts further investigations and produces a report on the

practice. The KPPU has the authority to summon the alleged businessman, along with witnesses, and to examine all documents. Finally, the KPPU gives a verdict; if the allegation is found to be true, then the KPPU imposes administrative sanctions on the businessman who has been judged to have broken the law of business competition (UU 5/1999 art.36). The administrative sanctions might be an order to stop the unacceptable practice, or could be compensation to the aggrieved party (UU 5/1999 art.47).

There are several practices that are regarded as unfair business competition: oligopoly, oligopsony, boycott, cartel, trust, vertical integration, secret agreement, monopoly and monopsony. The first, oligopoly, is assumed when few companies dominate production (seller) and acquire 75% of the market share of a product (UU 5/1999 art.4). Oligopsony is the same as the oligopoly, but with domination on purchasing side (buyer), which cannot be more than 75% of the total market share (UU 5/1999 art.13). Monopoly and monopsony are similar to these, but these situations only involve a large seller and buyer, respectively, who dominates more than 50% of the total market (UU 5/1999 art.17 & 18). By holding such dominating positions, the companies might regulate price in supply or purchase (UU 5/1999 art.1). A boycott can be created when a businessman makes an agreement with his competitor to refuse to buy or sell other competitors' products (UU 5/1999 art.10). Similarly, a cartel is initiated with an agreement that is intended to regulate prices by controlling the production and marketing of products or services (UU 5/1999 art.11). A mechanism of trust is the basically the same as a cartel, but the agreement is realised in a syndication of these competing enterprises (UU 5/1999 art.12). Vertical integration is an attempt to dominate a particular market by controlling its production chain (UU 5/1999 art.14). However, a monopoly is still allowed if it is related to public needs and managed by a state-owned enterprise (UU 5/1999 art.51).

The other new oversight body created during the reformation era is the PPATK (*Pusat Pelaporan dan Analisis Transaksi Keuangan* / Centre for Financial Reporting and Analysis), which is regulated by UU 15/2002, was revised by UU 25/2003 and then revised again by UU 8/2010. The UU 15/2002 is the legal basis for establishing the PPATK as an independent institution intended to deter and eradicate money laundering offences (UU 15/2002 art.1). The centre is responsible to the president (UU 15/2002 art.18), and it is therefore funded by the national budget (UU 8/2010 art.63). However, as an independent body, the work of the PPATK cannot be legally interfered with by any parties, including the president. The PPATK is allowed to cooperate with any

parties, both national and international, in attempts to deter and eradicate money laundering (UU 15/2002 art.25), such as by providing education and training regarding the technicalities and prevention of such an offence (UU 8/2010 art.41). Meanwhile, regarding international cooperation, the PPATK ratifies the international standard of the Financial Action Task Force (FATF) on money laundering in order to deter and eradicate money laundering and terrorist funding. This initiative is known as the revised 40 recommendations and 9 special recommendations (Revised 40+9) FATF (UU 8/2010, explanation).

The PPATK is tasked with gathering, filing, analysing, and evaluating information concerning suspicious financial transactions, and then reporting such information to the police and prosecutors if there is any indication of money laundering. A suspicious financial transaction is indicated when it falls into one or more of the following categories: financial transactions that deviate from a usual pattern; financial transactions that evade obligatory reporting of a financial service provider; and financial transactions that are allegedly the result of a criminal offence (UU 8/2010 art.1). In addition, the PPATK is responsible for providing recommendations to the government on how to combat money laundering, and also for producing accountability reports for the president and parliament every semester (UU 15/2002 art.26). The PPATK has the authority to undertake these tasks by asking for further information and documents from financial service providers. The PPATK has the right to conduct an audit of the financial service providers regarding compliance with guidelines concerning statements of financial transactions. In such a situation, provisions relating to bank secrecy and confidentiality of financial transactions do not apply (UU 15/2002 art.27). If the financial institution has been found guilty of breaking regulations, the PPATK has the right to impose penal and administrative sanctions (UU 8/2010, explanation).

The PPATK suggested that money laundering can be undertaken in several ways. The first is known as *placement*, which means that cash from a criminal offence is put into the financial system, particularly the banking system. The second is known as *layering*, which means transferring ‘dirty money’ that has been put into the banking system to credit the accounts of other parties, wherever they are located. The third is *integration*, in which the ‘dirty money’ that has been put in the banking system is used in legal business (UU 15/2002, explanation). Apart from the PPATK, there is a body which is named the *Lembaga Pengawas dan Pengatur* (Supervisory and Regulatory Agency). This agency is responsible for ensuring compliance with obligatory reporting

by financial services providers; the results of the agency's monitoring reports will be passed to the PPATK (UU 8/2010 art.31).

Another new oversight body is intended specifically to deal with corruption, collusion, and nepotism (KKN / *Kolusi, Kolusi, and Nepotisme*). In the early stages of the reformation process, the GoI established the Commission of Investigators of Government Officials' and Ex-Government Officials' Wealth (KPKPN / *Komisi Pemeriksa Kekayaan Penyelenggara Negara dan Mantan Penyelenggara Negara*) as an independent body that has responsibility for preventing KKN practices (UU 28/1999 art.1). Thus, government officials were required to disclose and publish details of their wealth before and after holding a public office position. A government official must be willing to be audited in the periods before, during and after he or she occupies an authoritative / powerful position (UU 28/1999 art.5). As an independent institution, the KPKPN's members were appointed by the president with approval from parliament; they are therefore responsible directly to the president (UU 28/1999 art.10-13). In addition, the investigation reports of the KPKPN must be available to the president, parliament, the BPK (as supreme auditor) and the Supreme Court (UU 28/1999 art.18). However, in August 1999, the GoI issued UU 31/1999, suggesting the transformation of the KPKPN into the Commission of Eradication of Corruption Act (KPTPK / *Komisi Pemberantasan Tindak Pidana Korupsi*) within two years (UU 31/1999 art.43). It has since been transformed again, from the KPTPK to the Commission of Corruption Eradication (KPK / *Komisi Pemberantasan Korupsi*) (UU 30/2002 art.2), but it still contains the same substance (UU 30/2002 art.3). However, the KPK has more extensive tasks that include the prevention of corruption acts, investigation, and prosecution in the special court of corruption (UU 30/2002 art.6). In terms of prevention, the KPK has the authority to disseminate information and education about corruption and to give input to the heads of agencies regarding administrative systems that are vulnerable to corruption (UU 30/2002 art.13-14). Meanwhile, regarding investigation and prosecution, the KPK has the authority to take over from police or district attorneys, particularly in a case that has not been followed up or has been interfered with by an executive body, the judiciary or legislature (UU 30/2002 art.8-9).

Corruption attempts are hard to prove when they involve cross-sectoral transactions, the use of sophisticated technologies, or government officials (UU 31/1999 art.27). In dealing with government officials, the GoI has set tighter regulations in UU 31/199 art.12, stipulating prohibition of using his/her position for personal benefit: for

example, receiving any gratification from another party in order to use his/her authority in favour of that party, in which the gratification will be regarded as a bribe (UU 20/2001 art.12). Thus, in order to deal with these situations, the KPK has broad authority, such as the power to intercept and record any communication, to forbid a suspect to leave the country, to obtain information from financial or other institutions regarding the financial transactions of a suspect, and to block the suspect's accounts. The KPK can also ask for assistance from Interpol to search, arrest and seize evidence from abroad (UU 30/2002 art.12).

The next effort to eradicate corruption was the establishment of special courts for the sole purpose of trying corruption offences; these are part of the public court and located in every province or district or city. The special court deals with cases of corruption and money laundering when that money is acquired from corruption or crime (UU 46/2009 art.2-5). The court is also required to disseminate information concerning trials of corruption to the general public (UU 46/2009 art.24). The special court is under the supervision of the Supreme Court, which also provides work plans and budgets for the special courts (UU 46/2009 art.33).

4.4.5. Interrelation of Local Governments with Stakeholders

Stakeholders of local government might influence the policies of the local government in various ways. The first stakeholder is the adjacent local government. Every local government is always bordered with at least one other local government, which sometimes raises some concerns regarding developments that might affect the other region(s). Therefore, the central government has produced a regulation in order to manage this concern. Regulation 22/1999 art.87 suggested building cooperation between local governments by establishing a joint agency as a communication media among adjacent regions. Moreover, this regulation also facilitates cooperation between local governments and more institutions than just other local governments. In 2004, this issue was reemphasised in regulation 32/2004 art.196 in order to achieve efficiency of public service management across regions. Government regulation (PP / *Peraturan Pemerintah*) 50/2007 gives guidance regarding funding for the joint agency by allocating it from the local budget.

Second, bureaucratic reform has recommended that the central government facilitate the involvement of local society in an effort to empower society regarding development (UU 22/1999 art.92), which is also known as society control (PP 20/2001

art.1). One method of involving local society is expected to be allowing input into the local government policy, as the local government is required to comply with UU 25/1999 art.27, as well as to disseminate information regarding the condition of the local government's finances. Therefore, the information is necessitated to be open data, which could be accessed and acquired easily by local society (UU 33/2004 art.103).

The other engagement by local society is in composing a work plan for the local government agency, consisting of policies and programmes that subsequently will be implemented by the agency (UU 32/2004 art.151 and art.199). The work plan of the local government agency (RENJA-SKPD) must refer to strategic planning by the agency (RENSTRA-SKPD) in accordance with the local government's mid-term programme (RPJMD) (UU 32/2004 art.151). The MoHA formulated mechanism of involving local society through discussion forums about development planning will be outlined in the work plans of the local governments (Musrenbang-RKPD / *Musyawarah Perencanaan Pembangunan – Rencana Kerja Pemerintah Daerah*) (Kepmendagri 50-187/Kep/Bangda/2007). The MoHA decree describes the Musrenbang-RKPD as a public event designed to obtain development priority and consensus from stakeholders to solve local development issues. This event is therefore regarded as a tool with which to synchronise and reconcile top-down and bottom-up approaches to community needs assessment and technical assessment. The Musrenbang-RKPD can be held in the form of public consultation, focus group discussion, or workshops. Stakeholders who are invited to this event are all stakeholders affected by development programmes, institutions that have an authority or vested interests in discussed issues, and representatives of local society. The stakeholders will be determined based on involvement in the discussed issues in term of contribution, resources and expertise. In addition, the local parliament is also expected to participate in this event, because planning and budgeting must be ratified by the local parliament before being implemented.

Involvement of the public is also expected in national institutions, such as in the KPK, the PPATK, and the KPPU. Active participation by the public is regarded as the right and responsibility of society, as part of an effort to realise clean governance. Public involvement may include providing information if irregularities occur (UU 28/1999 art.8-9), and the government will provide rewards to any member(s) of the public who assist with the prevention, eradication, or disclosure of corruption (UU 31/1999 art.42). Information from the public is also needed in relation to KPPU, as it

monitors business competition in order to eliminate monopolies or any other unfair business competition (UU 5/1999 art.3) or matters related to money-laundering crime (UU 8/2010 art.44).

4.5. The Influential Parties According to the Local Government Officials

Appendix 11 shows that the several parties affecting capital expenditure decisions can be classified into three major groups: regulators, oversight bodies, and stakeholders. The first element, ‘regulators’, refers to ministries that issue regulations affecting local governments, especially some aspects of mechanisms of control in the capital expenditure of local governments. The second element is ‘oversight bodies’, which engage with local government in attempts to ensure the implementation of government regulations. The third element is ‘stakeholders’, comprising several parties that are identified by respondents; these are state-owned companies, adjacent local governments, local society, NGOs, mass media, and suppliers/vendors. Each of the elements is described in the following sections.

4.5.1. Regulators

Ministries affect local government agencies in many ways, depending on the relationship of each ministry to the agency. For example, the MoHA (Ministry of Home Affairs) has the most important role in regulating local government, especially related to local government structure and all aspects of administration, as expressed by an interviewee:

There are ministerial decrees (Permendagri and Permenpan) related to management control systems regulating things that are supposed to be done by local government and local government agencies in implementation, planning, and budgeting. (SFO 2)

As mentioned in the quotation, the MoHA issues ministerial decrees, particularly Permendagri 13/2006, that is initial elaborations of government regulation PP 58/2005. The ministerial decree is a complete guideline to local government finance, encompassing all aspects of it, including structure, composition through to implementation, amendment of and accountability reports on the local budget, cash management, administration, accounting, mentoring, and supervising. Later, several articles of this ministerial decree were revised by Permendagri 59/2007, followed by a second amendment in Permendagri 21/2011.

Meanwhile, the Menpan (Ministry of Empowerment of Government Officials and Bureaucratic Reform) became involved in the organisational control system by issuing Permenpan 20/2010 as a basic road map of bureaucratic reforms from 2010-2014, encompassing macro, meso, and micro levels. The ministerial decree emphasises the following programmes: revamping organisational structure, management of human resources and operational procedures, and strengthening monitoring, performance accountability, and quality of public services. Moreover, the Menpan also issued ministerial decree Permenpan 05/2008 regarding audit standards for internal auditors, which involved several institutions, such as the BPKP, the inspectorate general for ministries, and the inspectorate of provinces and districts/cities.

In an attempt to strengthen the control system, the MoF (Ministry of Finance) has also become involved by issuing ministerial decrees Permenkeu 76/2008 regarding accountancy and financial reporting, particularly for the BLU (*Badan Layanan Umum* / Public Service Agency), such as regional public hospitals that can be categorised as BLU. Meanwhile, for local government in general, the MoF issued PMK 4/2011 as guidelines for the dissemination of information about local government finance. Particularly for specific allocation funds (the DAK), every year the MoF issues a ministerial decree for the forthcoming fiscal year, such as Permenkeu 201/2012 for the fiscal year 2013.

Apart from the ministries discussed above, related ministries also issue ministerial decrees to be implemented in that ministry's area. For example, the Ministry of Public Works issued ministerial decree 17/2012 in order to regulate performance accountability (LAKIP / *Laporan Akuntabilitas Kinerja Instansi Pemerintah* / Performance accountability reports of government institutions) for all institutions under the control of the Ministry of Public Works, such as the local government agency of public works. This situation also occurs in other ministries as part of an effort to improve performance in the respective ministries.

Although these ministerial decrees are intended to enhance the accountability of government institutions, these conditions are perceived to be overlapping each other, adding a significant burden to government officials, as stated by one senior financial official: "The regulations sometimes have the same intention, but these are 'packaged' in different ways. Consequently, this is troublesome for us" (HOA 3). This perception was also supported by an agency secretary who perceived that those regulations have

the same meaning but are expressed in different ‘language’ (SOA 13). However, the overlapping, and therefore the redundancy, are not total but only apply to some aspects of the regulations (SOA 11).

However, other local government officials have different perceptions than the previous critical views presented. Some perceived that all regulations are well coordinated and complemented each other, as suggested by one senior agency secretary (SOA 6). This perception was also emphasised by an inspectorate official who stated there is no overlapping in these regulations (SPO 16). However, there is another opinion, from a senior secretary of a local government agency, which pointed out that: “in the beginning, regulation is adjusted [to account for recent developments]; subsequently, it will always be adjusted again and again”. (SOA 12)

These varying perspectives confirm that local government officials differ in opinion. The overlapping perceptions can be triggered by two causes from two sides: on one side, local government officials are not well informed about the whole picture of the policies of central government, along with the regulations following the policies, because “central government representatives in a region do not really understand those regulations comprehensively” (SPO 16). On the other side is the fact that ministries are not well coordinated when it comes to issuing particular regulations: “those of us who work at an ‘operational level’ feel that regulations produced by each ministry are uncoordinated and those regulations are intended to work in the interests of the ministry.” (HOA 3). It has also been suggested by secondary sources that this can be attributed to ‘ministerial ego’. Meanwhile, the other perspective, -that is, the complementary perspective-, is that government officials perceive all ministerial regulations to be efforts to strengthen control mechanisms.

Any particular ministry may also affect a local government agency by implementing a particular software application in the planning process which enables each local government agency to propose its needs via the application process. However, the proposal must be in line with the available menu in the application. In addition, the related ministry may affect the local government agency by giving a grant in the form of equipment or tools to local government, which in some cases raises confusion among local government officials, as exemplified as follows.

The machine [a back-hoe] is extremely big, whereas we mostly need it in areas with small roads. So, it cannot travel along them. (SIA 1)

For example, we just received a car, but it is central government [ministry] asset... it is not supposed to be maintained from the local budget, because it is not recognised as being our asset. However, in this context, we have to maintain it, because we need it. (SOA 6)

Three years ago, the ministry gave us computers for our villages, but currently they do not work anymore. We even have higher spec computers. (SOA 7)

In this way, the local government agency can be perceived as being used by the ministry as a ‘destination,’ a way of spending the ministry’s remaining budget in order to achieve its target.

4.5.2. Oversight Bodies

Oversight bodies in the Indonesian government consist of many institutions, but interviewees in this study have identified four oversight bodies that affect local government officials when a decision is being made. The first oversight body identified by most interviewees is the BPK as the external auditor, which is highly respected by local government officials because the BPK performs audits regularly (SFO 2). Its audit opinions will affect local governments as a whole.

The BPK performs an audit every year and we are always selected as an audit sample...we are afraid of making any mistakes, because the BPK will produce audit reports. If [they find that] we do not ‘comply’ [with laws and regulations], we can go to jail. (SFO 8)

Moreover, the BPK staff are perceived to be very strict regarding regulations; many of its personnel are still young and very idealistic (SIA 1). The BPK will audit all the accountability reports of local government agencies (SOA 6), starting with planning and contracts, and will make physical checks if required (SIA 2).

Meanwhile, the second oversight body identified is the BPKP, an internal auditor which is much more engaged in the supervision and monitoring of administrative aspects of local government agencies. Local government agencies are regarded as having close relationships with the BPKP because, as a central government official, the BPKP representative is placed in a particular local government for several years to give assistance to that local government:

We are well acquainted with the BPKP staff because their rotation is quite slow compared to the BPK, which is so fast. As a result, we have become friends, good friends. They [the BPKP staff members] have different characters to the BPK [members]. (SFO 8)

The BPKP enhances its assistance by running training and coordination workshops for local government agencies, especially related to new regulations (SOA 6). Moreover, the assistance tends to be more related to the operational level, rather than the theoretical, such as determining indicators for the accountability reports of local government agencies (SPO 12).

The third oversight body identified by interviewees is the KPK (Commission of Corruption Eradication). Although the commission has close relationships, in terms of its operation, with the PPATK (Indonesian Financial Transaction Reports and Analysis Centre) and the KPPU (Commission of Monitoring of Business Competition), the focus of local government officials is more on the KPK than the other institutions. The reason for this orientation is that the KPK might be investigating any suspicious transactions; in the recent past this has resulted in many heads of local governments or heads of local government agencies going to jail. Hence, now local government officials are much more careful than previously when making any expenditure decisions. Consequently, budget absorption also tends to be lower than in the previous era:

Recently, the KPK has become very focused [on fighting corruption], we always remind all local government agencies every time we hold a meeting to use the budget in accordance with regulations. Any hesitance can be discussed with the inspectorate or the BPKP. We always monitor the incorporation of the budget; if it is still low, we will remind them [the local government agency]. (HOA 7)

In addition, one of the central government agencies, indicated by an interviewee, is the UKP4 (*Unit Kerja Presiden Bidang Pengawasan dan Pengendalian Pembangunan* / Presidential Work Unit for Development Monitoring and Control), which comes directly under the supervision of, and is responsible to, the president:

Concerning financial control, there are many layers. For example, we have to report to Jakarta, to UKP4. Every month we do reconciliation; every three months we will be checked by inspectors. And so we are inspected monthly, quarterly, every semester, and yearly. (SPO 7)

Recently, performance reports for the UKP4 have been intensified. The reports will be monitored and evaluated regularly by Bappeda (*Badan Perencanaan dan Pembangunan Daerah* / Regional Body for Planning and Development) (SOA 14).

4.5.3. Stakeholders

Interviewees of this study identified several stakeholders that are considered to be important when engaging in decisions about capital expenditure. The first and most

identified stakeholder by the interviewee is local society, which will be impacted directly by a project. Local government has two different ways of acquiring input from local society: formal and non-formal. The formal method can be accommodated through Musrenbang (*Musyawarah Perencanaan Pembangunan* / Development Planning Forum) held by the executive, or a *jaring asmara* (*Penjaringan Aspirasi Masyarakat* / public aspiration gathering) (SPO 4; SOA 2). Then, all input will be distinguished based on authorities' positions in the hierarchy [i.e. central government, provincial, or municipal (SPO 9)] and will be considered in the budgeting process based on the financial capability of local governments (SFO 7). Although sometimes this process does not meet the criteria for being efficient and effective, the input from the public might be included in the budget if it is perceived to be really needed by local society (SOA 5).

Apart from the formal approach, every local government agency employs different ways to absorb feedback from local society, such as by email, or message services at any time (HOA 1; HOA 6). One of the non-formal approaches is that providing direct input to the head of local government when visiting a particular area. Another method is by submitting a proposal to the administrative development agency. Then, all inputs, both formal and informal, will be listed, verified, and ranked based on the priority of a particular area or local government agency, or the local government as a whole (SPO 4; SPO 15; SOA 12). In addition, local society is able to participate directly in development processes, either by providing a grant in the form of a building (HOA 6), or through other fixed assets (SFO 11). Then, all grants from the public will be recognised as local government assets (SFO 11).

The input from local society will subsequently be put into the budget and then implemented. Afterwards, the impact of the development as realisation of the budget will be assessed for evaluation (SOA 7; SOA 12). However, as time goes by, the impact of a project may well decline; for example, the development of a bus station that is rarely used nowadays because the public prefers to use their own vehicles, or the closure of many schools due to the success of a nationwide family planning programme (it is suggested that each family have a maximum of two children) (HOA 7). Moreover, local society is also able to engage in this formal assessment through the IKM (*Indeks Kepuasan Masyarakat* / Index of public satisfaction) (SPO 3). However, the IKM has been perceived sceptically by some government officials because it is assumed that the public will not give a bad assessment to a local government agency. The reason for this

is that the public often engages with a local government agency or agencies and they therefore have a good relationship, either personally or institutionally, which they will not wish to spoil (SPO 9).

The second stakeholder is an adjacent local government, or governments, because a local government might have a border with one or more local governments, thus necessitating the sharing of concerns or responsibilities (SOA 9); it needs to be determined who will handle what (SPO 14). In order to deal with this issue, the provincial government established a joint secretariat as a place for coordination, known as '*Kartamantul*', which is an abbreviation of Yogyakarta, Sleman and Bantul (SOA 9). The joint secretariat is also expected to reduce any tension among local governments, as stated by one local government official:

We have two or more heads of local government with the same authority, but they have different interests. Sometimes, this causes open disagreement; hence, the existence of the joint secretariat is required to reduce the impact of these differences. (SOA 8)

In addition, the secretariat is very useful as a medium for municipalities to communicate when dealing with financing difficulties related to infrastructure that will affect other regions (HOA 1).

The third stakeholder is non-governmental organisations / NGOs, which monitor procurement processes (SOA 5) or any other local government expenditure (SPO 9). Hence, local government officials unavoidably engage with them (SFO 10):

Now, it depends on implementation, precision, and accuracy; so far, there has been no spurious claim. [By this] I mean that, all projects are implemented [realised], and all goods [the results of the implementation] are in place according to specifications. Here we have specific NGOs, for monitoring or independent monitoring system.....sometimes, a project supervisor is afraid of it. Well, as long as we comply with regulations this, we don't have to be afraid. (HOA 7)

However, not all NGOs really know (or are fully up to date with) particular regulations and specific guidelines related to local government expenditures (SPO 5).

The fourth stakeholder is the mass media, which in several local governments involves TV, radio, and newspapers. Any news published in those media might attract the attention of one or other of the oversight bodies, and might be followed up with an investigation:

When the '*TRIBUN*' newspaper published news of a suspicious irregularity occurring in the project, the BPK straight away came to investigate the case. That is the reason why we are afraid to see any official or unofficial letter regarding a

project. Even any rumour that has been published in a newspaper might put us in trouble. (SFO 14)

As well as informing on any irregularities, mass media can be used as a means of communication between the heads of local governments and local society; radio is particularly useful for this. For example, members of the local community could complain about the condition of infrastructure or any public services (HOA 5).

4.6. Summary

This chapter discusses the engagement of many parties outside of elements of local government in the control of capital expenditure. Furthermore, it also depicts the interrelationships among these external parties. This study signifies three important points: that rivalries among regulators are likely to occur; that local government officials tend to focus on oversight bodies that have the authority to impose sanctions, including prison; and, finally, that all stakeholders of local government has their own agenda, in which they tend to work independently and are not interrelated with the identified stakeholders. The first and second points have a strong connection because the oversight bodies play a role in maintaining the compliance of local governments towards regulations that have been issued by regulators, such as ministries. Meanwhile, most of the stakeholders, at least officially, do not have a strong relationship with either regulators or oversight bodies, although unofficially they can and do interact with both government institutions. For example, if it is indicated that fraud is likely to happen, one of the stakeholders might report this possibility to the relevant oversight body or ministry, which will duly investigate the report.

To summarise, this chapter illustrates an attempt at domination in the production of regulations by regulators and the cultural response of local government officials towards the domination, which tends to be conservative. Meanwhile, the oversight bodies play its roles as ‘police’ which emphasis on control and disciplinary of local government institutions. Finally, the roles of stakeholders need to be empowered as complementary to the oversight bodies; this is due to the limitations of the resources of the oversight bodies compared to the number of overseen subjects.

The external parties along with their interrelationships are explored in this chapter; the following chapter then discusses the interactions of internal elements of local government in the capital expenditure process, along with the obstacles they face and the way these are dealt with.

Chapter 5

Engagement of the External Actors with Local Government Apparatuses in the Capital Expenditure Processes

5.1. Introduction

The previous chapter identified external parties that influence capital expenditure decision-making. Participants in this study identified several parties that were later categorised into three groups: regulators, oversight bodies, and stakeholders. The involvement of these actors can be perceived as the interference of international institutions in order to establish transparency and accountability in public finance, as outlined in several Letters of Intent. This move has significantly affected many aspects

of local government practice, such as decentralisation policies, direct elections of heads of local governments, reinstating and empowering of current oversight bodies, establishing new oversight bodies, constituting government accounting standards, empowering local society, and implementing many best practices adopted from the private sector.

This chapter aims to highlight changes in regulations related to capital expenditure processes, along with the engagement of external parties in implementing these processes. The implementation of capital expenditure processes encompasses planning, implementation of that planning, and monitoring of full processes; external parties may engage with any of these stages. In addition, this chapter also takes into account several issues regarding local government characteristics that might affect these stages. Therefore, the sampled local governments were previously classified based on the specific characteristics of each region; for example, the breadth and character of the area, its poverty level, the minimum education levels of local government officers, and the average capital expenditure from 2010-2013. The classification of the local governments is intended to emphasise specific problems emerging in specific regions, especially in the procurement processes.

This chapter begins by looking at changes in capital expenditure policy, which is followed by a description of the impact of these changes on several aspects of the capital expenditure process, such as many parties engaging in capital expenditure decision-making, developing planning of capital expenditure, and mechanisms of procurement and selection of suppliers. The next section is a description of the sampled local governments, encompassing profiles of the regions, particularly their geographic conditions, the distribution of rural and urban areas in each region, leading sectors in the regions, and the education levels of the local governments' civil servants. Furthermore, this chapter presents the impact of the regulation changes on the sampled local governments, particularly in the planning, selection of suppliers, execution and monitoring stages. The final section is the summary of this chapter.

5.2. Changes to Regulations Concerning Procurement

Regulations concerning procurement in local government have been developing over time. Regulations to establish financial control in Indonesian local government were initiated in the “New Order” era, because the “Old Order” era still relied on regulations inherited from the Dutch. The evolution of the regulations

concerning financial control, especially capital expenditure, which is derived into presidential decrees, is set out in appendix 12. The government of Indonesia has passed several presidential decrees regarding procurement processes, including capital expenditure.⁴ The several revisions from the initial presidential decree are undertaken by considering the dynamics within the context of government organisation, which, shifting from centralism to decentralism, are reflected significantly in the procurement system. In the pre-reformation system, which adopted the centralistic model, approval of a project depended on the value of the project. The higher the value of the project, the higher the level of approval that was required. For example, this approval could come from a particular minister, or from the coordinated ministries of economics, finance and development, as reflected in the presidential decree 24/1995. Meanwhile, in the post-reformation era, the procurement system has reflected a decentralisation perspective, because approval is not based on the value of a particular project, but rather on the overall local government budget, by taking into account its financial capabilities.

In the post-reformation era, the initial presidential decree is number 18/2000, which encompasses many aspects of procurement and lays the foundations for undertaking procurement professionally by firmly setting out the mechanisms of procurement. These mechanisms are still employed to date; nevertheless, they have been improved through the adoption of e-procurement, a modernising development underpinned by presidential decree number 54/2010. The information presented in appendix 12 indicates that regulations that evolve from time to time tend to become stricter, because job assignments that used to be centralised with heads of local governments are reduced and distributed to other parties, such as the ULP or a procurement committee, along with clear descriptions of the roles and responsibilities of each party. This procedure is designed to increase the transparency of procurement processes, as authority is not concentrated in one party anymore. In addition, in order to enhance transparency, the LKPP was established by presidential decree 54/2010. This decree was then followed by the establishment of the ULP, under the supervision of the LKPP; these moves are expected to improve procurement practices that used to be undertaken manually and which are perceived to be open opportunities for collusion between government officials in authority and suppliers. The presidential decree

⁴At first, the Government of Indonesia passed presidential decree number 18/2000, which was amended by presidential decree number 80/2003, and revised by presidential decree number 54/2010. In 2012, the presidential decree was reviewed and then revised again by presidential decree number 70/2012; the latest revision is presidential decree number 172/2014.

54/2010 accentuated the establishment of the ULP (*Unit Layanan Pengadaan* / Procurement service unit) in local governments, which had to be established by the fiscal year 2014 at the latest. This unit is required to support implementation of the e-procurement that was introduced in the fiscal year 2012, embracing e-tendering and e-purchasing.

5.3. Mechanism of Procurement of Capital Expenditure

5.3.1. Roles of Local Government Officials in Capital Expenditure

Procurement involves many parties, both within a local government agency or external to the agency, which is depicted in appendix 13. Those involved within the agency include the PA (*Pengguna Anggaran* / Budget user), which usually refers to the head of that local government agency. The PA delegates his/her responsibility, which used to be handled by the treasurer of a local government agency, to the KPA (*Kuasa Pengguna Anggaran* / Deputy of the budget user). When the particular local government agency requires something, the KPA might delegate authority to the PPK (*Pejabat Pembuat Komitmen* / Committing Officer) to determine the requirements of the goods/services. After the PPK has determined the requirements, he/she submits the findings to the ULP (*Unit Layanan Pengadaan* / Procurement Service Unit) or to procurement officers.

The ULP has the main responsibility for handling all procurement documents that have been handed over by the PPK (*Pejabat Pembuat Komitmen* / Committing Officer) and is responsible for determining the specification of the procurement based on the requirement of the local government agency. The ULP handles the procurement of goods/services/construction works worth more than IDR100 million (approximately equal to USD7000), a figure that was revised by the presidential decree 70/2012 by increasing the baseline to more than IDR200 million (equal to roughly USD14,000); and above IDR50 million (approximately equal to USD3500) for consultancy services. Consultancies are considered to be a different service because this term is used to identify design consultants and supervisory consultants in construction projects.

Meanwhile, capital expenditures valued at less than IDR200 million for construction, and worth less than IDR50 million for consultancy services, are handled by procurement officers with a direct appointment or direct procurement mechanism. In order to ensure the procurement is undertaken professionally, the PPK and procurement officers must be certified for public procurement by the LKPP (*Lembaga Kebijakan*

Pengadaan Barang/Jasa Pemerintah / Agency for policymakers of government's procurement of goods/services) as an administrator at the national level.

5.3.2. Mechanism of Planning of Capital Expenditure

The reformation that has been undergone has provided a fundamental change in terms of the relationship between central and local government. In the previous era, the central government used to control procurement by local governments, especially for high-value projects, but now all procurements are under the control of local governments themselves. Moreover, the procurement process also offers more opportunities for the involvement of local society in decision-making which affects them, as well as controlling the performance of local government officials, as the local government now has more power to manage resources in order to provide public services for local society (Purba, 2010).

The mechanism for procurement starts when the local government agency identifies its needs through various means, either via internal identification or through input from external sources. The internal needs are identified through internal meetings, which must conform to programmes outlined by related ministries. After the internal meeting, the identified needs are submitted through e-planning applications to the related ministries. Any needs that are not listed in the menu of software applications cannot be submitted to the related ministry. Meanwhile, the external inputs are acquired from several sources, such as *Musrenbang* (*Musyawarah Perencanaan Pembangunan* / Development planning forum with local society), *Jaring Asmara* (*Penjaringan Aspirasi Masyarakat* / Acquiring aspirations of local society), hearings with the local parliament, and direct input from local society to the related agency. Afterwards, based on the identification, all of these proposals are ranked and prioritised in the RUP (*Rencana Umum Pengadaan* / Master plan of procurement), when implementation of the selected programmes is based on the budgets of related organisational units. Subsequently, the relevant organisational unit produces a DED (Detailed Engineering Design) before it is submitted to the ULP.

In this mechanism, another factor that must be taken into consideration is the roles of the local parliaments. Since the reformation, the members of local parliaments are elected directly by local society; the members have strategic functions towards local government (executive), for example as a partner in governing. One such function is legislation that initiates drafts of local regulations and/or gives approval to drafts of

local regulation that have been proposed by the executive. The approved draft of the budget will then become the budget implemented by local government. In most cases, the local government will need to amend the budget that has been approved by taking into account the recent circumstances of the local government. The local parliament often approves amendments to the local budget in the last quarter of a year, a requirement which puts a local government under pressure because it must prepare all the processes of capital expenditure within a very limited time. This situation requires local government officials to make difficult choices. On the one hand, they are required to meet local government budget targets, but on the other hand, they also have to meet public expectation regarding the quality of assets or infrastructure.

After the budget has been approved, the PA (budget user) composes a master plan of procurement (RUP); then the PA delegates the authority for the implementation of the RUP to the KPA and the PPK, who carry out the programmes. The PPK must specify the goods/services based on their requirements. After the procedure has been completed, it is handed over to the ULP in order to be put into e-procurement for the procurement of goods/services totalling more than IDR200 million or IDR50 million for consultancy services. Meanwhile, any procurement below those limits is handled by the procurement officials of a local government agency.

5.3.3. Procurement and Evaluation Methods of Suppliers' Proposals

Procurement can be undertaken through two methods: self-managed and selection of suppliers of goods/services. The self-managed method involves planning, implementing and supervising the procurement, which is being undertaken by an agency. In terms of construction work, this method only encompasses rehabilitation, renovation, and simple construction. Complicated construction is undertaken by a particular agency and, when it has been completed, it is handed over to the local community/society as a user. In order to ensure the implementation of the project in terms of effective utilisation of the budget, the involvement of the APIP, which is responsible for internal audit, is required. The second method is procurement involving a third party, as a supplier of goods/services.

Selection of the third parties is undertaken in several ways, particularly in the selection of suppliers involved in construction works: for example, by general auction, limited auction, direct selection, direct appointment, or direct procurement. First, the most common method is a general auction with several requirements. Second, the

simple selection is specified for procurement with limited suppliers involving complicated work. Third, for simple construction worth up to IDR200 million (approximately USD14,000) a supplier can be selected straight away if the supplier meets the qualification. Fourth, direct appointment can be applied in specific circumstances, such as in a state of emergency. Finally, direct procurement is specified for procurement up to IDR100 million, or about USD7000, and involving small and medium enterprises as a supplier.

Proposals that have been submitted by suppliers are selected by the ULP based on a single-elimination system, a value system, and economic life cycle cost. The first system is the single-elimination system, which is the most common system employed in procurement; exemption is given for projects with high complexity, costing above IDR100 billion or USD7 million, which require the application of a value system or valuation cost of economic life as the evaluation method. The single-elimination system is based on the assessment of suppliers' proposals through verification and comparison between the proposal and requirements that have been set. Any suppliers that cannot meet the requirements are eliminated. The second method is a value system that is measured by assigning point values for each element that has been set, based on specified criteria and weighting. Then the total values are compared with the suppliers in order to decide which one has the highest value. The last method is economic life cycle cost, which assesses suppliers' proposals by employing point values for technical elements and price, referring to economic life based on particular criteria and values that have been established. This method is applied to highly complex projects, as it also considers operating costs, maintenance costs, and the residual value of the assets.

Meanwhile, for consultation services, the ULP uses four methods for selecting consultants: an assessment based on quality; quality and cost; budget ceiling; and the lowest cost. The first method is an assessment based on the quality of technical proficiency, which is initially verified and then continued with negotiations involving technical matters and fees. The second method is based on an assessment of quality and cost, in order to select the best combination of both components (i.e. the quality of the technical service being offered and its price). The third approach, which is an evaluation based on the budget ceiling, is when proposals are compared with the budget ceiling; selection is normally based on the value of the proposals, with the one offering the lowest price selected. Finally, an evaluation based on the lowest value is also used to select a consultant with higher technical standards than are required.

Each of these methods can be applied to a particular project; for example, assessment based on quality is applied to the selection of consultants for a macro perspective, or planning and supervising projects of high complexity, such as the construction of a power plant, an underwater tunnel, or an international airport. Assessment based on quality and cost can be applied to projects that are less complex than the previous mega-examples; for example, a primary irrigation system, road, feasibility study, project consultant, or a construction which does not involve building. The next method of assessment, based on the concept of the budget ceiling, can be applied to construction projects, both for planning and supervising the construction of a building. The final method, based on the lowest cost, is employed in simple projects, such as the design and supervision of simple buildings.

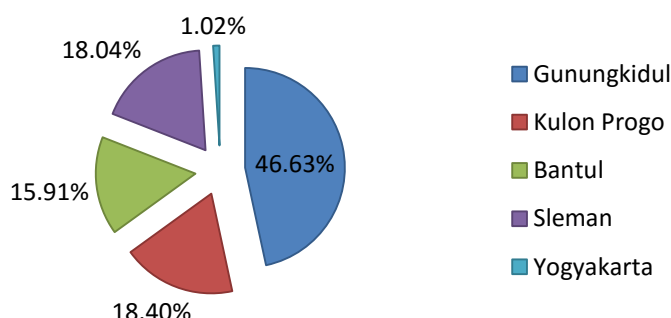
After passing through stages of assessment, the ULP then decides the winner of the auction. However, the ULP still gives the other suppliers an opportunity to appeal regarding this decision. The supplier who appeals against this decision must give a deposit worth 5% of the contract value, or HPS (*Harga Perkiraan Sendiri* / Self-estimated price), or a maximum of IDR50 million (equal to USD3500); this provision was revised by presidential decree 70/2012 to be worth 1% of HPS. Otherwise, the ULP offers the contract to the winner of tender. When the supplier signs the contract, they must also give a security deposit worth 5% of the contract's value or of the HPS.

5.4. Issues with the Procedures of Procurement in Particular Local Governments

5.4.1. Brief Profile of the Sampled Regions: Geographic and Demographic Conditions

The Special Region of Yogyakarta (DIY) province is located in the centre of Java Island and consists of five local governments; these are the districts of *Gunungkidul*, *Bantul*, *Kulon Progo*, *Sleman*, and *City of Yogyakarta*. The percentage of the total geographical area of each local government relative to the Yogyakarta Province is as follows: *Gunungkidul* 46.63%, *Kulon Progo* 18.40%, *Sleman* 18.04%, *Bantul* 15.91%, and *Yogyakarta* 1.02%, as presented in Figure 5.1. Approximately 65.65% of the area is situated at a height of between 100m and 499m, 28.84% at a height of less than 100m, 5.04% at 500m–999m, and 0.47% at a height of 1000m or more (D.I. Yogyakarta, 2014).

Figure 5.1. Percentages of total geographical area by districts or city in the D.I. Yogyakarta province



Source: *Badan Pusat Statistik D.I. Yogyakarta (Central Agency on Statistics of the Special Region of Yogyakarta), 2014, p.7*

Figure 5.1 shows that the *Gunungkidul* district is the largest area in the province of *Yogyakarta*, while *Kulon Progo* and *Sleman* are approximately the same size. These are followed by *Bantul* and, finally, the smallest region, which is the city of *Yogyakarta* itself. Most parts of the districts of *Gunungkidul* and *Sleman* are located at an altitude of between 145m and 185m because these regions contain hilly areas, and there is a volcano in the *Sleman* region in which situated at an altitude of more than 500m. Meanwhile, the districts of *Bantul*, *KulonProgo*, and *Yogyakarta* are mostly situated at altitudes of between 45m and 75m.

Each of the five regions administers sub-districts and villages, made up as follows: *Kulon Progo* consists of 13 urban areas and 75 rural areas; *Bantul* 47 urban areas and 28 rural areas; *Gunungkidul* 5 urban areas and 139 rural areas; *Sleman* 59 urban areas and 27 rural areas; *Yogyakarta city* 45 urban areas. Based on this distribution, the district of *Gunungkidul* has the largest area, and most of this area is rural (95%). This district is the farthest from the centre of the province of D.I.Yogyakarta. The district of *KulonProgo* is the second largest in terms of area, and the second furthest in terms of distance from the centre of the province. Therefore, both of these regions can be regarded as outer areas in this study. Meanwhile, the district of *Bantul* is the third farthest from the centre of the province. Finally, *Sleman* is the closest district to the centre of the province, and is situated adjacent to the city of *Yogyakarta* (D.I.Yogyakarta, 2014).

In addition, as presented in appendix 14, in the districts of *Gunungkidul* and *Kulon Progo*, 54.41% and 50.24% of the population, respectively, rely on the

agriculture sector. Hence, in these regions, there are many rural rather than urban areas. Meanwhile, the district of *Bantul* is about to shift from being an agricultural sector (16.98%) into manufacturing (21.78%), as well as being involved in trading and tourism (26.55%), the latter involving the development of hotels and restaurants in the region. The development of financial services involves about 20.95% of the total population of *Bantul*. Finally, the district of *Sleman* relies on trading, hotels, and restaurants as leading sources of income and employment (28.54%). The city of *Yogyakarta* itself depends on trade, hotels and restaurants (47.57%) and services (26.28%) (D.I.Yogyakarta, 2014).

All of the above conditions are set out in appendix 14, which emphasises the shifting orientation of the local societies of these regions from the agrarian sector to industrial and trading sectors. The data give insights into the conditions of the local societies, where the agricultural sector is representative of traditional society, while the industrial and trading sectors indicate modernised society (Charlton and Andras, 2003). According to these criteria, the *Gunungkidul* and *Kulon Progo* regions can be classified as traditional societies when compared with the other regions. On the other hand, *Bantul* and *Sleman* are shifting from traditional into modern societies, while the city of *Yogyakarta* can be classified as representing an already modernised society. The different types of society might react or behave differently towards specific conditions, particularly in terms of social boundaries in these two societies. A traditional society is depicted as a pyramid of top-down authority, while a modern society is exemplified as a mosaic that is put together with mutual interdependence (Charlton and Andras, 2003).

Moreover, demographic conditions regarding civil servants in each region reveal evidence that a few officers in the local governments still have only the minimum level of education, as summarised in appendix 15. Civil servants at the provincial level, who have minimum level of education, make up 42.46% of the total; in the *KulonProgo* that figure is 31.56%; in the city of *Yogyakarta* it is 28.98%; in *Gunungkidul* it is 28.29%; *Sleman* is 26.39%; and the lowest figure comes from the district of *Bantul*, with 26.22% (D.I.Yogyakarta, 2014). The officers' education levels are an important factor; they are perceived to affect the way local governments apprehend and resolve the problems they encounter (Pakpahan et al., 2014). Moreover, Charlton and Andras (2003) suggest that the process of modernising society can be accelerated through education. At the organisational level, an employee's standard of education affects the job satisfaction of that individual, which will in turn influence the level of employee

turnover (Lambert et al., 2001). It has been suggested that this happens because a person's education has other functions apart from technical requirements, for example as a socialisation medium and for transmitting occupational values (Gusfield, 1957).

The figure in appendix 16 shows the distribution of civil servants based on their levels of education, and indicates that most civil servants are educated to degree level. Approximately 40% of civil servants in the five local governments are first-degree holders, apart from in the *Kulon Progo* district, where the figure is 36%. The high number of degree-holders in this figure can be accounted for by the fact it is the minimum requirement for civil servants in order to be placed in middle management (Indonesia, 2013). The middle management is responsible for the operation of capital expenditure processes, from the start up to the handing over of the procured assets. Hence, this chapter considers the relation between the demographic conditions affecting socio-culture in specific regions and the role of education levels in local government cultures in order to determine how this contributes to the creation of an atmosphere conducive to work.

5.4.2. Economic Conditions and Capital Expenditures of the Regions

All municipalities of *Yogyakarta* province still depend financially on funds from the central government, both from the DAU (*Dana Alokasi Umum* / Generally allocated fund) and the DAK (*Dana Alokasi Khusus* / Specifically allocated fund); this constitutes, on average, around 64% of total revenue. Regional revenue that can be generated by the municipalities totals about 14%, and the rest comes from other sources of revenue, such as grants, emergency funds, and provincial funds. Of the total expenditure, most (approximately 57%) is assigned to pay civil servants' salaries, except in the province of D.I.Yogyakarta, which allocates only 20% of its funds to personnel expenditure. About 12% of total outgoings is allocated for capital expenditure, as presented in appendix 17, which includes the capital expenditure of all sampled regions since 2010 - 2013 (D.I.Yogyakarta, 2014).

Capital expenditure in every region in the Province of Yogyakarta is presented in appendices 17 and 18. From 2010-2013, all regions experienced increasing capital expenditure, except the two largest districts: *Gunung Kidul* and *Kulon Progo* slightly decreased their expenditure in 2013 from that in 2012. As the largest districts, both regions would be expected to spend more on capital expenditure in order to accelerate development in these districts (Adi, 2006; Harianto and Adi, 2007). Meanwhile, the

city of *Yogyakarta*, which only has a small area of around 1% of the total area of *Yogyakarta* province, in 2013 allocated IDR121,557 million (about USD8.7 million) for capital expenditure, an increase of 42% from 2012. The district of *Sleman* and the province of *Yogyakarta* increased their capital expenditure substantially in 2013 compared to 2012.

All of the conditions of the sampled local governments are summarised according to their areas, along with the conditions of poverty, education levels, and capital expenditure in each region, in Table 5.1.

Table 5.1. Classification of the regions along with the socio-demographic conditions

Area	Rural		Semi-urban		Urban
Region	Gunungkidul	KulonProgo	Bantul	Sleman	City of Yogyakarta
Percentage area of district or city	46.63%	18.40%	15.91%	18.04%	1.02%
Percentage of rural areas	96.52%	85.22%	37%	31%	0%
Poverty	21.70%	21.39%	16.48%	9.68%	8.82%
Minimum education level	5.01%	3.99%	3.23%	2.73%	5.73%
Average capital expenditure 2010-2013 (in IDR million)	154,229	94,087	108,094	127,115	84,083

The table above indicates that the district of *Gunungkidul*, which has the largest area, also received the largest allocation of capital expenditure. However, the ‘total area’ does not necessarily receive a proportional allocation of capital expenditure; the district of *Kulon Progo* has the second largest area, but receives a relatively small allocation for capital expenditure. Meanwhile, the other regions receive a proportional allocation for capital expenditure.

5.4.3. Internal Dynamics of the Sampled Local Governments

Managing the vast amounts of money allocated for capital expenditure requires managerial skills from the heads of local governments or the heads of local government agencies, particularly in order to formulate procurement plans that benefit local communities. The role of leadership is considered to be an important aspect, as indicated by one official: “If the head of an organisational unit does not understand a new system, he/she will give unclear and biased instructions to their subordinates” (SOA 13). Although the role of leadership is perceived to be crucial, in cases of

promotion to head of an organisational unit, far more value is currently placed on seniority than meritocracy: “Seniority is the main consideration for a job promotion, without considering the competency and job experiences of the candidates” (SPO 12). The competency and capabilities in the head of the organisational unit are really needed in order to foster a dynamic organisation: “We have an organisational unit head, who has good ‘processor’ and ‘storage’ [abilities]; hence, we help her by supplying her with data recording applications” (SOA 12). Moreover, leadership is required in order to build an organisational culture, as it is noted that organisational culture must be established firmly and started by the superior officer. This is typified by a senior financial officer scrutinising the decision of central government to increase the limit of procurement, which might increase opportunities for misconduct:

This system is much better because user and vendor do not contact each other directly. As a result, the procurement committee is not afraid of being contacted by vendors. However, a problem arises because the threshold of e-procurement is IDR200 million, which means that procurement below IDR200 million can be arranged directly, giving the organisational unit a wide-ranging opportunity to ‘play’ [i.e. try to get money for their own]. At the national level, IDR200 million is a relatively small amount, but for local governments, it is quite large. Therefore, many local government agencies try to set procurement below IDR200 million in order to avoid e-procurement, allowing the organisational unit will be able to choose which supplier they wanted. (SFO 5)

The officer indicates a practice that might occur in a local government agency. He has points out how an agency might use the regulation for their own benefit, as direct procurement requires the supplier to provide commission for unscrupulous persons in an organisational unit in order to secure the project. Furthermore, he suggests that this practice is quite common in organisational units and that the occurrence of the practice strongly requires that the head of agency deal with it: “if the head of agency intends to ‘play’ [in the procurement], then the subordinates will follow and to ‘play along’ as well” (SFO 5). This example therefore affirms the importance of the roles of heads of agencies in building an organisational culture within their agency.

The larger area, which consists of rural areas such as *Gunungkidul* and *Kulon Progo*, offers other challenges for the head of an agency, because the staffs rely heavily on the head to create an effective local government agency, as stated by one senior planning officer:

The head of an agency will give directions to their subordinates through the civil servants’ ceremony and by making a personal approach, person to person....and sometimes even, structural boundaries are omitted. The relationship will rely on friendship and brotherhood, ties that we can remind each other about.

Coordination is maintained whenever we go to take any action; all coordinators will gather to discuss a plan of action...However, the effectiveness of this approach is not as expected (SPO 5).

Furthermore, semi-urban regions, such as in the districts of *Sleman* and *Bantul*, start to become more independent and professional. However, the roles of heads of agencies are still to dominate in order to control their subordinates: “He comes to our offices every week and asks us: how is your work?...And we hold a meeting: Monday for the finance division and Tuesday for other divisions” (SPO 1). Meanwhile, in the urban region, comprising the city of *Yogya* and province of *Yogyakarta*, the staffs tend to be more independent at work. Although all decisions are made by the heads of agencies, staff can provide suggestions based on their expertise, and even dare to argue with their superior, as exemplified by an interviewee who creates an indicator of output measurement:

It must be clear what the improvement is, what the initial condition was, what should be measured, what are the parameters. I formulate this and apply it to the Renstra [Strategic planning]; then it is adopted by the Bappeda [Local government planning agency], and all agencies are required to adopt this method. (SPO 12)

This example shows that initiative is encouraged and appreciated in this case, because what the officer created was later adopted by the planning agency (Bappeda) and prescribed for use by all other agencies. In another case, one of the interviewees describes how he argued with his superior regarding the implementation of a software application:

We had spent a lot of money to develop this system [SIPKD], but they [the supplier] wanted us to switch to their system and they came to the provincial secretary, but the secretary asked me about it. I argued with them to show me the weaknesses of our system. If they were vital, I did not mind changing [the system]; if they were not vital, I asked why I had to change it....that was a glimpse of a software application that would affect our internal control (SFO 14).

Both examples demonstrate critical thinking by the staff, which tends to be more developed in urban areas than in rural or semi-urban areas, and an egalitarian atmosphere is more noticeable in the urban context. For example, when group interviews were conducted involving heads of divisions and secretaries of agencies, they argued with each other regarding some topics, without restraint, even though their superior was also in the same room. This is an atmosphere that was not found in other peer interviews in rural or semi-urban agencies.

5.5. Compliance of Mechanisms of Procurement to the Regulations

5.5.1. Formulation of Capital Expenditure Planning in Local Governments

Regarding the implementation of planning mechanisms, every agency might have different ones because they are under different ministries. Each local government agency is under the supervision of related ministries and each agency undertakes programmes handed down from the ministries. In order to control capital expenditure, the ministries apply different methods; for example, a local hospital that is under the Ministry of Health employs e-planning, whereas the transportation agency that is under the control of the Ministry of Transportation implements different software applications. Hence, every agency must comply with the regulations of at least three ministries, i.e. Ministry of Finance and Ministry of Home Affairs for all agencies, and related ministries for specific agencies. This somewhat complex arrangement sometimes raises problems, as indicated by several sources. The various ministries have their own programmes that must be implemented right down to district and regional level; however, among those ministries, there appears to be a lack of coordination.

In general, “at the beginning of a fiscal year, we submit a proposal to the relevant ministry [Ministry of Transportation]” (SPO 6). The proposal must refer to Renstra (*Rencana strategis* / Strategic planning) as long-term planning: “So, core and master plan have been set; hence, any replacement of the head of local government will not affect the policy because all developments must refer to the master plan, which is specified within the yearly programmes afterwards” (SOA 7). In addition, the master plan becomes a reference for the priority of programmes (SPO 6):

For capital expenditure, such as that funded by the DAK [Specifically allocated fund], technical guidelines will usually accompany it, along with menus for its application. Each agency is only able to propose in conformity with this menu. So, we are constrained by this menu; even if we need something, we cannot propose it because it is not available on the menu. (SPO 3)

Then “the internal meeting is needed to prioritise the needs” (JPO 1). After the technical guidelines have been examined, the meeting will be held, chaired by the head of an agency, in order to determine which one should be prioritised (SFO 2). Afterwards, “when the master plan of procurement (the RUP) has been accomplished, and the DED has been acquired, the following next year will then involve suppliers being selected through an auction in the ULP” (SOA 7). This mechanism has been implemented widely in local government agencies. Although they have implemented the procedures as required by regulations, in the same way, the intensity is different due to the different circumstances encountered by each particular agency. For instance, three interviewees

were from agencies under the supervision of the same ministry, but they came from different local governments, representing the three regional categories (rural, semi-urban, and urban). Although they came from agencies under the same ministry, because they came from different regions, they posed different challenges. Issues arising in the rural area, with regard to the planning stage, were mostly related to human resources:

This is related to a presidential decree, and we have provided guidelines. The certified staffs are supposed to understand the presidential decree, but in one particular case, they cannot understand how to handle it. For example, procurement in 2012 was delayed because there was no solution; we could not take any action without any legal basis. (SPO 6)

This situation indicates the importance of continuous improvement for and of human resources, especially for certified staff who handle procurement processes. Such personnel must always be updating their knowledge regarding new regulations issued by the government.

Meanwhile, the semi-urban regions face a different problem, as described: “For the planning system, in every section, we have a planner...and he synchronised the district programmes with our agency, and every division has a technical planner” (SOA 7). However, this model is not always as successful as expected, particularly when it does not take into account the dynamics of society, as confirmed by the other interviewee from the same region:

There is a public transport terminal; we do not know the future, it was built before [the time when] motorcycles and cars can be purchased easily through leasing. Therefore, people prefer to ride a motorbike because they consider it cheaper than public transport. Hence, the terminal cannot be utilised optimally. (HOA 7)

This particular example indicates that planning, specifically long-term strategic planning, might not fit with the dynamics of society. Therefore, the aspirations of local society must be noted seriously, not only in order to meet the regulation that must be adhered to. The involvement of local society / communities in planning is also needed in order to overcome issues that are encountered in the urban region, because conditions in the urban region are more dynamic than in the rural or semi-urban regions. Hence, the agency is both required and obliged to adjust with the dynamic: “Planning changes are very dynamic and very fast, but they must be accommodated in the Renja [*Rencana Kerja* / Yearly planning]....if there is a change, we have to consider our capacity to accomplish it by the end of the fiscal year” (SPO 10). Through the involvement of the local community, the expenditure can be expected to be utilised optimally by society.

It is a regulatory requirement to involve local society in order to gain input that subsequently will be considered in composing the local government's budget, although the government agencies' work is based on strategic planning (Renstra) within a 5-year time frame, which is then narrowed down into yearly planning (Renja):

Basically, the five-yearly vision and mission is elaborated upon within yearly programmes, and in the yearly programmes, we hold onto something that can provide aspirations for society, i.e. Musrenbangdes, Musrenbang kecamatan, Musrenbang kabupaten, then the provinces, and then finally at the national level. Therefore, we have a database of society's needs...Then, we prioritise by considering: what is the most important thing for society, whether the location is strategic or not, and whether it stimulates the surrounding areas or not. (SOA 7)

Hence, any input from local society must conform to the Renstra; otherwise, it will be omitted. This reflects the fact that public involvement in capital expenditure decision-making is limited, although the central government has been providing media for the public to channel their aspirations regarding capital expenditure through MUSRENBANG (*Musyawaharah Perencanaan Pembangunan* / Public participation in development planning) as a public consultation forum. However, the outcomes of the MUSRENBANG are not satisfactory, as the public is not well informed about the availability of resources, which has created a cynical perception of this event: "It makes the participants dream. They are encouraged to say whatever they want, and finally, in the end, I will make the decisions about what can be done, based on how much money I have" (Purba, 2010). This means that MUSRENBANG can be perceived as a mere formality, and is regarded as an instrument of legitimacy.

In addition, it should be pointed out that the availability of an up-to-date database is also perceived to be an important issue: "the technical database of government infrastructure is required as the basis for budgeting and planning programmes, but we do not have accurate and updated data" (SPO 4). A planning officer suggested that "data in central and local government are not valid at all" (SPO 9). This situation is very confusing: on one side is a substantial technical database, but on the other side the validity of this database is seriously questioned. Data regarding one subject can differ from department to department, as exemplified in the following comment: "data for healthy housing, from the public health office, are different from the public works department; data regarding irrigation of agricultural areas from this organisation unit differ from data supplied by the agricultural organisational unit" (SPO 9). In addition, the officer suggested that this dissonance might occur because of the application of different methods or due to a different understanding of the same subject.

5.5.2. Selecting a Contractor or Supplier of Capital Expenditure

After the general planning of procurement (RUP) is composed by the head of an agency, it is delegated to the PPK in order to be implemented, either through direct procurement or by submission to the ULP (*Unit Layanan Pengadaan* / Procurement services unit) for procurement by tender. Some agencies prefer all their procurement to be put through the ULP, for reasons such as a lack of certified procurement staff or in order to reduce psychological pressures, as the suppliers tend to approach the staff who handle the procurement process. However, other agencies prefer to handle their own procurement decisions. One reason for this is that there is a limited time frame for putting a procurement tender through the ULP, while the agency is required to meet its budget absorption target.

Improvements in software applications have stimulated development in the capital expenditures mechanisms of local governments, through the employment of e-procurement. However, levels of implementation of the e-procurement model vary among local governments, who come to depend on the ULP as organiser of the e-procurement, because of confusion regarding regulations that must be complied with, as indicated by a senior financial officer: “City [of *Yogyakarta*], [District of] *KulonProgo*, *Sleman* have established the ULP; we [Province of *Yogyakarta*] are still in the process [of establishing it]” (SFO 14). Local governments view the ULP as part of various local government agencies: “The ULP cannot be attached arbitrarily to any agency, the DPPKA or Bappeda [*BadanPerencanaan Pembangunan Daerah* / Local government development planning agency]” (SOA 10). Therefore, establishing of the ULP must refer to a specific ministerial decree:

Referring to the Ministerial Decree of Kemenpan (Ministry of apparatus empowerment and bureaucratic reform) regarding its main duties and functions, the LPSE (*Layanan Pengadaan Secara Elektronik* / E-procurement services that organised by the ULP) is supposed to be coordinated by Bappeda in the controlling division. However, when the ministry issues an official letter that is because the LPSE is related to the [software] application; therefore, it must be put under the coordination of the transportation, communication and information agency [*Dinas Perhubungan dan Kominfo*]. In other provinces, it is placed in the supplies bureau, but we do not have such a bureau. (SPO 17)

In addition, the ULP as the organiser of the LPSE (*Layanan Pengadaan Secara Elektronik* / E-procurement services) requires personnel who hold certification for the procurement of goods and services. However, certification has also become a problem for several local government agencies because only a very limited number of

persons meet the requirement for certification: “[the number of] procurement staff is very limited” (SPO 3). This point is also supported by an agency head: “even though it is not obliged by regulation [because procurement is below IDR200 million]; I prefer to give [the project] to the ULP because we only have two certified [procurement] staff” (HOA 5). An issue that has arisen within many local government organisational units, which do not have sufficient personnel with appropriate qualifications, is also stressed by a local official: “for the technical team, we rely on personnel from other organisational units. We have proposed four persons, but only approved one” (SIA 1). This deficit condition has occurred in many organisational units in many local governments; workloads of certified officials are therefore quite high.

After the procurement is announced to the public, procurement staff select suppliers that have submitted their proposal by considering many aspects, such as technical requirements, price, and the reputation of the supplier. Blacklisted suppliers are not allowed to participate in procurement tender, or to be appointed as suppliers. However, the availability of an up-to-date comprehensive database regarding this issue is very limited; suppliers have ways of overriding the current system, which is why many blacklisted suppliers are still able to participate in the tendering process or manage to be appointed as vendors. Moreover, support and oversight from professional associations are inadequate; hence, the blacklisted suppliers are still able to operate: “each municipality has its own blacklisted suppliers; blacklisted suppliers from one region might win a tender in another region” (SFO 4). This negative situation indicates that the database was built for a specific local government and has not been integrated throughout even a province. This situation is highly favourable for ‘bad’ suppliers. On the other hand, professional organisations, which purport to regulate a specific profession, appear not to play any role in enforcing the appropriate code of ethics: “professional organisations are required to do so; they should have control of the members of the organisation. We have suggested it, but it seems they do not bother about it” (SFO 14).

Ideally, increasing levels of decentralisation should result in increasingly effective control systems, which improve the performance of particular local governments through the implementation of suggested changes. It is essential that decentralised decisions must be supported by the availability of *valid* information as feedback for the decision maker (Miah and Mia, 1996; Glynn and McCrae, 1986). Distorted information leads to misallocation of resources, and thereafter results in the

diversion of management attention away from the economy, efficiency and effective accomplishment (Smith, 1989). Thus, the availability of an integrated database is necessary in order to meet the challenge in the public sector, where compliance with regulations, public accountability and public expectation is perceived to be more important than in the private sector.

5.5.3. Implementation of Procurement of Assets

After a vendor or supplier has been chosen through the selection process, they become responsible for the execution of the project. The project executors can be distinguished into three types: planning consultant, contractor, and supervising consultant. At the first stage, a local government agency determines the technical specification, administrative requirements, and qualifications of tender participants (SPO 11). Then, in the technical planning stage, a local government agency is involved in supervising and reviewing, especially with regard to specifications and site conditions (SPO 4), because sometimes the planning might be implemented in a remote area or even on a mountain (HOA 4).

The next stage in the implementation of a project is the construction stage. If there is any input from local society as users, it can be accommodated by considering technical and financial conditions (SFO 4). In the construction stage, the supervising consultant plays an important role in ensuring the quality and specification of the construction. Hence, the involvement of local government officials is required in order to reduce the possibility of collusion between the contractor and the supervising consultant (HOA 6). If a local government official finds a discrepancy between the planned specifications and the real conditions, the situation will be discussed together with the planning consultant, the contractor and the supervising consultant (HOA 6). Meanwhile, any delays in the completion of a project will have different consequences, the worst being the unilateral termination of the contract (SPO 4).

5.5.4. Monitoring the Implementation of Planning by Many Parties

The procurement processes attract the attention of many parties in order to ensure the process is run fairly: “we try to solve any problem with the ombudsman and with non-government organisations as well” (SPO 1); this is basically to ensure that the lowest bidder is chosen as the winner of the auction. However, one senior financial officer offers a different opinion:

The procurement committee members are afraid if they do not choose the lowest bidder because the BPK will question it. Choosing anyone but the lowest bidder will be regarded as a waste of public funds. Therefore, the regulation does not support the committee choosing supplier who offers better quality. (SFO 14)

This statement indicates that the officials see themselves as being ‘in the middle’. On one side, they are pressed by the public and other stakeholders to provide a good quality service; on the other, they are required to spend at the lowest level by regulations imposed by the BPK (*Badan Pemeriksa Keuangan* / Indonesian Supreme Audit), which acts as external auditor for government institutions.

The inspectorate, as one local government institution that has responsibility for internal audit, also plays an important role in supporting improvement control in local governments. However, the inspectorate’s involvement varies. In one region, it is perceived to be insufficient by an organisational unit: “we coordinate with the inspectorate for evaluation, but the inspectorate cannot coordinate regularly” (SFO 3). Meanwhile, in another region, the involvement of the inspectorate is quite intense: “staffs of the inspectorate are more focused on building link with organisation units. This helps us to be more organised in terms of administration and compliance with regulations” (SOA 9).

Therefore, procurement through the ULP is perceived in a positive way as it reduces psychological risk: “procurement risk is related to psychological risk as well. Many persons come to my office asking about the procurement process; that places great pressure on us” (SOA 2). Even an officer in an organisational unit tends to forward any procurement decisions to the ULP (*Unit Layanan Pengadaan* / Procurement services unit) in order to reduce this risk: “if all procurements were able to be put to auction through the ULP, we would be happy to do that, as we get pressure from many parties, such as the BPK, the BPKP, the district attorney, the police, and the mass media” (HOA 5). This suggests that some officials want to shift their ‘burden’ to the ULP, as the pressure from many sources has tended to increase recently. They do not want to be put ‘in the middle’ between public expectation and regulatory requirements, especially when the local budget needs to be amended: “the amendment of the local budget is usually in September or October; while for capital expenditures need to be put on auction. Time is limited [and so an agency does not dare spend it], so no wonder budget surpluses are high” (SFO 10). This notion explains the involvement of local parliament as a representation of political parties, the members of which pursue

their somewhat selfish agendas with considerably more energy than is seen in their commitment to their constituents (Choi, 2004). Since the public sector is closely related to a country's political context; hence, the relationship might trigger a conflict of interests (Mayston, 1992). This is consistent with that of Abdullah and Asmara (2006), who noted the occurrence of opportunistic behaviour by local parliamentarians in order to satisfy their needs. Therefore, if an agency urges that the budget be spent, the agency must face the consequences: "time restrictions make expenditure higher, as expenditure must be prepared in only three months" (SPO 10). However, in order to deal with this problem, an officer may try a risky way to manage the budget through estimation and planning, including regarding the procurement processes being undertaken in advance. Yet the expenditure must only be carried out after receiving approval from the local parliament, as expressed in the following statement: "I will spend more than budgeted, which includes the budget surplus in this spending, but implementation of the spending of the budget surplus must be suspended until approval from the local parliament" (SOA 3).

5.6. Summary

This chapter presents descriptions of a range of planning processes implemented by local government agencies. It also considers geographic, demographic and socio-cultural conditions, which vary in every region and which also affect planning processes. Therefore, this chapter emphasises how the planning processes are affected by socio-cultural variables and values inherited from the previous era; behaviour and values that have been institutionalised in local government officials. In addition, demographic conditions must be considered in this study, as demographic factors also have an effect on socio-cultural change. Therefore, the sampled regions in this study are categorised as rural, semi-urban and urban areas.

The findings of this study indicate the importance of the head of an agency as the leader in its organisation. However, public servants in rural areas tend to rely heavily on the head of the agency, a role whose importance decreases in urban areas, where the officials tend to work independently in an environment that also tends to be more egalitarian. This study also found that every sampled agency implemented the same approach to instructing subordinates; an action that is performed through *apel* or formal ceremony. This regular practice was designed to establish the loyalty of government officials, and emphasises the hierarchical relationship between superior and

subordinates rather than the managerial skill or leadership of the head of a local government agency. Such a notion will become an obstacle to the creation of an egalitarian atmosphere in Indonesia's government offices, which is apparent in the rural areas that are less egalitarian than the urban regions.

Regarding the mechanism of procurement planning, each region also encounters different problems. In the rural regions, the most apparent issue is a lack of certified procurement staff to handle procurement processes. Meanwhile, in the semi-urban and urban regions, civil servants are trying to deal with the dynamics of a society that is changing at a rapid pace. However, all the regions encountered a common issue: the involvement of local society/communities in designing procurement planning, via MUSRENBANG, as required by regulations. Local input is 'taken on board' in order to meet the requirement of regulations, rather than actually obtaining real input from local society. Moreover, the unavailability of the integrated database that is needed for technical planning and blacklisted vendors also raises another troublesome issue for local governments.

Dealing with procurement makes the local government agency the centre point of pressure from many parties, such as the civil society organisation, the ombudsman, the district attorney, the police, the BPK (Indonesian supreme auditor), and the local parliament; this encourages the local government agency to give up all selection processes to the ULP. This arrangement is expected to reduce the unwanted psychological pressure and stress being experienced by the agency officials. Regarding relationships with the local parliament, on one side the local government officials are required to meet the budget; on the other side, they must deal with amendments to the budget that are approved in the last quarter of each fiscal year by the local parliament, which gives them only a very limited time in which to complete the capital expenditure project.

Chapter 6

Summary Discussion of Key Findings

This study has identified the most influential parties, and how those parties affect capital expenditure control at the local government level, based on the perception of local government officials. Respectively, this study has specified many parties involved in stages of capital expenditure decision-making, both formal institutions and non-formal bodies, along with various interests as outlined in Chapter 4. Then, this study demonstrated that every party tends to use its power to achieve its own ends, and explored how local government officials deal with those intentions, as discussed in Chapter 5. The empirical results demonstrate that various intentions from various parties tend to either strengthen or weaken the control mechanisms in many ways, which is summarised in this chapter.

Bureaucratic reforms initiated in 1999 affect many aspects of government, both at national and sub-national level. One reform initiative was related to decentralisation, which gives more independence to local government to control and authorise their own expenditure. It means that currently local government has broader decentralisation and manages much more funding than in the previous era. In the previous era (the “New Order” regime) ministers were highly reliant on decisions made by the president. Structurally, the ministries were based on a military model, because the president and most of the ministers had a military background, while governors and heads of municipalities also tended to have a military background. Furthermore, the influence of the president on parliament was enormous, which made the position of the president very strong. In this condition, based on hierarchical military order, the president was able to coordinate national and sub-national levels. Rivalry among ministries was unlikely because it could be eliminated by intervention from the president. Hence, military hierarchical order was an important aspect of control and coordination in the “New Order” regime.

After the reformation, direct elections were introduced for the appointment of the president, vice president and heads of local governments, at both provincial and municipal levels. Consequently, the president, vice president and heads of local government come from diverse backgrounds. Ministers could be chosen based on merit, with the result that many professionals were chosen to be ministers. The military hierarchical order that had been established by the “New Order” regime could not be implemented in the post-reformation era. Moreover, the intervention of political parties at the ministerial level has made interrelationships among ministries more complex than in the previous era, which was dominated by a single party. Hence, new mechanisms of control and coordination are urgently required in this era to supersede the military hierarchical control.

This study has shown that many local government officials of sampled regions perceived competition among regulators as an attempt by ministries to dominate local government in an expression of the ‘power’ of central government. One of the attempts at domination is represented by the issue of ministerial decrees in relation to local government expenditure: the main ministries, which hold responsibility for local government, tend to establish their domination by decree, although in several aspects

the ministerial decree might contradict decrees from other ministries, as indicated by several government officials.

The other attempt at domination, especially by a ministry relating to a particular local government agency, comes in the form of giving a grant to the related agency, which use to be in form of fixed assets. The local government agencies deal with receiving equipment from related ministries as the programme of a particular ministry is implemented. The allocation of equipment in some cases poses another problem for local government agencies; for example, the equipment may not fit with local government needs because they were not tailored to the geographical conditions of the local government. Hence, the equipment is abandoned without use. Equally, the specification of the assets may be inappropriate for the local government's current requirements and in some cases may not have been needed by the agency. This situation occurs because a related ministry is required to meet its budget targets; the ministry must spend its budget, therefore they must issue a related local government agency with a grant in the form of fixed assets. This can create situations that are quite problematic for the specific local government agency, as depicted by the interviewees in the Chapter 4.

In another case, there was a problem regarding recognition of the fixed assets in a local government's financial statement. The fixed assets in a form of equipment coming from a ministry were delivered directly to local users without the related local government agency being notified. Consequently, the equipment was recognised as an asset by the user in its financial statement, but not by the local government agency that oversees the recipient institution. In a similar instance, equipment from related ministries were not officially handed over to a specific local government agency; the equipment therefore cannot be recognised as assets of that local government agency and cannot be maintained from that agency's local budget.

Two oversight bodies had been established during the "New Order" era, namely BPK (the Indonesia supreme auditor who act as the external auditor of central government) and BPKP (the internal auditor of central government). Meanwhile, other oversight bodies were established during the reformation era. During the "New Order" era, the roles of BPKP and BPK tended to overlap. The BPKP, which was supposed to focus on internal controls and build financial systems, emphasised the audit function and thereby encroached on the BPK's area of authority. All strategic sectors were

audited by the BPKP, such as oil and gas, the central bank, and state-owned enterprises. In this era, the role of the internal controller was concerned not only with financial control, institutional performance and corruption eradication attempts, but also the political or ideology orientation of government officials (Nasution, 2009). Following the reformation agenda, the traditional roles of the BPK were reinstated and it assumed the position it is supposed to occupy.

Moreover, the GoI established several oversight bodies in light of the recommendation of the international institutions that has been imposed in the letter of intent (LoI). For example, the LoI of 10th April 1998 Par.15 endorses the implementation of a law relating to business competition as an attempt to enhance market efficiency by placing emphasis on fairness in business practices and the suppression of anticompetitive behaviour. Later, this suggestion was realised and reinforced by the LoI of 16th March 1999 Par.45, which prompted the GoI to establish the KPPU (Commission of Monitoring of Business Competition) in order to eliminate monopolistic practices and unhealthy competition. Thus, the law placed more emphasis on the actual behaviour of businesses than on market structure, which is imposed by a judicial process along with penalties.

Another suggestion that was outlined in the LoI of 16th March 1999 Par.40 was the introduction of the KPK (Commission of Anti-corruption), which was expected to be operational by early April 1999. The KPK has responsibility for combating corruption in the public sector and reporting it to parliament, the Supreme Court and the president. It was later endorsed by the LoI on 14th May 1999 Par.31, which suggested that the law should be issued by 28th May 1999 and become effective within six months, with the interim period to be used to strengthen the institutional infrastructure of the commission. Another oversight body that was established during the reformation era was the PPATK (Indonesian Financial Transaction Reports and Analysis Centre) by referring to the LoI of 14th May 1999 Par.41, with responsibility for preventing money laundering along with authorisation to obtain information about foreign exchange transactions, capital inflow and outflow to and from any financial institutions in Indonesia.

This study shows that all of these institutions have clearer roles during the reformation era than during the previous era, and that they complement each other. However, of the identified oversight bodies above, most local government officials pay

more attention to the BPK and the KPK than to the other oversight bodies. None of the local government officials were aware of involvement of the KPPU and the PPATK in the control mechanisms. Meanwhile, the BPKP is regarded as a working partner of local government officials, with whom they can discuss and seek consultation on any problems related to the implementation of rules and regulations. However, local government officials tend to be very careful when engaging with either the BPK or the KPK, because these oversight bodies are perceived to have legal implications, as well as authority, if there are any suspicions of financial irregularities.

In addition, regarding stakeholder involvement, in the previous era the stakeholders did not have a significant role in any local government decision-making. Local society, NGOs and mass media did not have the opportunity to speak up about their needs or participate to control local government's spending. Meanwhile, the vendor or contractor selected for a project was often closely related to a very important person in either local or central government. None of the stakeholders criticised these practices. However, empirical findings indicate that the current roles of stakeholders have become clearer following the reformation movement. For example, roles of local society have been elevated, although in some cases it is still regarded as ceremonial in order to fulfil a regulatory requirement. NGOs have also been endorsed, and consequently many new NGOs have been established in this era. In addition, mass media is also guaranteed by freedom of the press to disseminate information to the public, and contractors are assured of fair competition when obtaining a project, because the KPPU has been established to support this practice, and stakeholders are actively involved in monitoring the procurement process.

This study shows that engagement of local government with the parties discussed above is conducted in various degrees of intensity in every stage of capital expenditure decision-making. For example, in the stage of capital expenditure planning, implementation of new regulations relies heavily on the heads of local government agencies, a phenomenon that is more obvious in rural regions, where society still upholds traditional values. Meanwhile, in semi-urban and urban regions, society is more egalitarian and therefore more willing to accommodate more dynamic relationships between superiors and subordinates.

On the other side, implementation of new regulations must be supported by competent and qualified staff, such as local government officers. In order to realise this

target, the LKPP requires all staff who handle the procurement process to be certified as procurement officials. However, conditions in many local governments, particularly in rural areas, make it quite difficult to satisfy the certification requirements, because of a lack of qualified personnel. This problematic situation cannot be resolved immediately, as all local governments, except for the provincial government, are affected by a recruitment moratorium policy. The moratorium imposes the requirement that personnel expenditure should not constitute more than 50% of that government's total budget. From the sampled regions, only provincial government passed the threshold, i.e. the personnel expenditure was below 50% of local government's total budget, whereas municipal governments did not pass the threshold, thus hindering them from recruiting new government officials. Therefore, the moratorium has inhibited the municipal governments' ability to meet the required number of officials that are needed for each local government agency based on job analysis results. In consequence, the municipal governments are only able to allocate 75% - 80% of the job analysis results.

In addition to the implementation of new regulations, the central government, through its ministries, employs technologies in planning procurements, such as e-planning. Implementation of e-planning has advantages and disadvantages for local governments. According to local government officials, the advantage of implementing e-planning is that it makes the planning process a lot easier, because the system has features to accommodate the complexities of the process. Hence, the planning process can be undertaken faster than before, because the proposed procurements are directed to the relevant ministry as soon as the data have been entered into the system. However, e-planning also has disadvantages; for example, a local government agency must stick to the procurement allocation that has been determined under a particular ministry and put it into the system in a form acceptable to the available menu. Any procurement proposal that deviates from the prescribed menu cannot be accommodated. Another problem has been identified by local government officials, and particularly concerns those local government agencies under the watch of several different ministries; the implementation of different e-planning for different ministries is accompanied by a variety of different requirements.

Another challenge, particularly for the planning process in the semi-urban and urban regions, is that it must deal with the rapid development of local society, a change that needs to be accommodated in strategic planning (*Renstra*). Inability to accommodate this development has resulted in the abandonment of either infrastructure

or equipment. This problem was exemplified by an interviewee regarding the development of a bus station, which was used for less than five years after its completion because of the shifting preference of the local community from buses to private vehicles; the bus station was ultimately abandoned. This case can be accounted for in two possible ways: one possibility is that the development was really needed but that a feasibility study conducted by the relevant agency did not consider the dynamic nature of local society; another possibility is that the development was not really necessary, but was merely undertaken in order to meet an expenditure target.

Involvement of local parliament is therefore needed to act as a counterpart to local government, particularly for giving input on the setting of budgets. In the previous era there was only one ruler, justifying an authoritarian approach; however, through the reformation movement, the position and authority of parliament at national or sub-national levels have been reinforced. The reformation has enabled the implementation of a multi-party policy, in which all members of local parliament are elected directly by local society. Many people want to become members of parliament, spending considerable sums of money in order to be nominated by a political party. Consequently, where local parliaments were initially expected to meet the expectations of their constituents as an expression of the democratic model, in reality, the opportunistic behaviour of members of parliament is more likely to occur (Abdullah and Asmara, 2006). This behaviour is particularly apparent in the approval process of the amendments of capital expenditure budget. Since, the local parliament used to approve the local budget in the final quarter of a fiscal year, which places greater pressure on local government agencies. This condition is common in the sampled regions, and it complicates the procurement processes, as the remaining time to undergo the procurement is only three months before the end of the fiscal year.

In Indonesia's reformation era, not only have the roles of local parliament been reinstated, but involvement of the local communities has also been encouraged; however, currently it is still at a superficial level, because a local government must stick to long-term planning instead of accommodating the aspirations of local society. Thus, the engagement of local community members in many arrangements can be regarded as an attempt to comply with regulations merely in order to legitimise the local government's planning; that is, long-term planning with little consideration of feedback from local society.

In this context, planning officials need to know what infrastructure has been constructed in order to be able to plan a more integrated development. However, the database of the local government's infrastructure is not available at the moment, which complicates planning and inhibits the development of subsequent infrastructure or maintenance planning for that infrastructure. In addition, the database is required because each local government adjoins other regions, and it is necessary to determine what belongs to whom. Thus, a local government will be able to make an allocation from its local budget for subsequent development, if required, or for the regular maintenance of that government's infrastructure. A further example concerns the maintenance of a road connecting two local governments, with the two sides of the road each maintained by a different government.

Regarding infrastructure in relation to other local governments, pressure tends to escalate when infrastructure affects another local government's income. This is exemplified by interviewees in this study who pointed out that the existence of a bus station in one area affected another local government's income, as the bus station is a source of income for the local government thanks to a levy on buses that pass through the station. The bus station was built right in the border, preventing others regions from building another bus station within a certain range. All the issues that might arise between the sampled local governments are resolved by the provincial government that oversees and administers these municipal governments. The provincial government established a joint secretariat to settle any issues that might arise among the overseen local governments. However, difficulties tend to become more complicated when those issues involve local governments from other provinces, because there is no specific institution to accommodate a conflict of this nature. It has to be resolved by involving the MoHA (the Ministry of Home Affairs).

Subsequently, the second stage of capital expenditure is the selection of a supplier or contractor. This can be undertaken in two different ways; by a procurement official in each local government agency, or procurement by a specific organisational unit of local government, such as the ULP. In the first method, procurement is handled by an official of a local government agency, and this is applicable when the value of procurement is less than IDR200 million. This value is regarded as considerable, especially for rural areas or regions covering a small area. Consequently, a lot of the procurement of assets is still handled by local government agencies. However, a differing perspective from a government official suggests that the threshold of

procurement might incite misbehaviour regarding the procurement process. A local government agency can split a 'big' project into several 'small' projects in order to enable collusion with suppliers/contractors.

In the second method, procurement is carried out by the ULP that is established in every local government and which applies different approaches to accomplishing the task of procurement. The level and quality of implementation of the ULP in each local government therefore varies. The ULP in each local government is overseen by the LKPP. The establishment of this body was intended to suppress collusion between local government and private sector officials, which used to occur frequently and was regarded as common practice. In addition, some officials of local government agencies perceive the procurement unit to be necessary in order to reduce the psychological pressure caused by the procurement process, as all such processes are now handled by the ULP. However, this effort is still in its early stages and needs to be improved in terms of the applied system and the personnel behind the system.

For the selection of suppliers, one of the supporting systems needed by procurement officials, both in the ULP and in local government agencies, is an integrated database of blacklisted suppliers. Currently, this kind of database is not available and the 'black' supplier might therefore be able to operate across local governments under different corporations, sometimes by 'hiding' behind another person's name as the manager or administrator of the corporation. By employing this modus operandi the supplier cannot be detected by the current system, and regulations cannot resolve this issue as it is not regarded as breaking the regulations. An official of a local government agency gave the following example: a corporation won an auction, but it was suspected that the corporation was operated by one of blacklisted supplier; the auction result was therefore annulled. As a result, the corporation appealed against the local government's decision on the basis that the business was administered under a different name than that of the 'blacklisted' supplier. However, the local government were able to prove their suspicion and upheld the decision. Meanwhile, the involvement of professional bodies, such as the Indonesia Contractors Association, in regulating its members is still very low. Actually, officials of local governments expect more engagement from professional bodies in providing input regarding this ethical issue and in imposing professional sanctions on any member who breaks their professional code of ethics or regulations.

The third stage of the process occurs after a supplier or contractor has been appointed: the supplier must sign a work contract before proceeding with their work. There are three external contractors involved in a project: a planning consultant, a construction contractor and a supervising consultant. The contractors also must provide a financial deposit, which varies depending on the value of the contract, as a precautionary measure in case the contractor fails to fulfil their obligations. The procurement official sets the terms of completion for every project; if the contractor cannot meet the terms of completion, then that contractor will be fined. The planning contractor is responsible for providing detailed technical drawings of a project, which will be realised by the construction contractor. In several cases, particularly in relation to the construction contractor, one of the main explanations for an inability to meet the terms of completion of construction was that the prices of building materials increased far more rapidly than expected, and the contractor was therefore unable to continue their work. Consequently, the contractor had to pay a fine and the project was listed again for auction. During the course of construction, every stage is supervised by the supervising contractor, who is responsible for providing procurement officials with reports on the progress of the project. In addition, construction can be unofficially monitored by users of the building, by members of local society who are affected by the project, or by NGOs. Any input or feedback from those parties can be accommodated, provided it meets with local government's technical and financial conditions. Otherwise, the project will be constructed based on the initial plan. Any discrepancies that might arise between technical planning and real conditions will be resolved by a meeting between the planning consultant, contractor and supervising consultant. This meeting will determine who will be held responsible for the discrepancies.

Besides the technical supervision, administrative supervision is conducted by an inspectorate, which is a local government agency that is responsible for being the internal auditor of local government. This agency is responsible for providing input on procurement processes by referring to current regulations; the inspectorate is approachable by any local government agency that needs to consult it regarding particular regulations. However, several officials of local government agencies perceive the inspectorate to be failing to employ a proactive approach. One reason for the inspectorate's difficulties is the insufficient number of personnel to cover all local government agencies. The role of the inspectorate as a local government's internal auditor is also supported by the BPKP, as the internal auditor of Indonesia's central

government. The BPKP has established a good relationship with local government agencies, according to many local officials. The BPKP works hand in hand with the inspectorate to supervise administrative tasks performed by local government agencies in terms of compliance with regulations. Furthermore, the auditing of all aspects of procurement, including planning, implementation and constructed assets, is the responsibility of the BPK as Indonesia's supreme auditor, acting as an external auditor in this sense. This institution audits the 'fairness' of all procurement processes, as well as assessing the 'fairness' of the relationship between the value of the contract and the constructed asset. In this audit, the value of the constructed asset will be checked physically. However, not all projects are audited by the BPK, as the number of BPK auditors is very limited compared to the vast numbers of local government agencies throughout Indonesia. Hence, the BPK mostly focuses on high value projects in particular local government areas. Being audited by the BPK is regarded as a key concern for officials of local government agencies, particularly for officials of finance departments, as any serious mistake will affect the auditor's opinion and could be followed up on by the KPK if the BPK found any indications of corruption in a project. Any such suspicion might therefore negatively affect the career of the local government agency official in the future.

Currently, informal bodies also play an important role in safeguarding procurement processes. One of the informal interested parties is the NGOs. Engagement of NGOs has become more active after the reformation era; NGOs are now able to monitor local government budgets and the implementation of those budgets. In particular, capital expenditure draws the attention of the NGOs, as it involves a vast amount of money. NGOs in several cases have approached a particular local government agency to 'discuss' the local government's implementation process, which puts more pressure on local government agencies to behave correctly. Therefore, officials of local governments need to be able to settle the NGO-initiated issue persuasively. Another source of informal monitoring is the mass media, which has also been affected by the reformation movement and now has more freedom to convey information to the public. An officer from a local government agency offered an example of when the mass media exposed a 'suspect project' based on a reporter's suspicion. It attracted attention not only from local society but from many other parties, such as the BPK, the district attorney and the police; thus, the project was probed. Currently, these two informal bodies (NGOs and mass media) are considered to be very

influential in shaping perceptions of asset procurement within local society. Meanwhile, the involvement of the district attorney and the police may be less than transparent, as suggested by an officer who implied that the involvement of the two authorities was motivated by a desire to get ‘money’, in order to ensure that the case would not be further investigated. Hence, in these conditions, a local government must be able to deal with many parties’ interests, both legitimate and otherwise.

To sum up, this chapter has discussed the external parties affecting local governments’ decisions in capital expenditure, including regulators, oversight bodies and stakeholders. In relation to the regulators, many local government officials perceived uncoordinated interaction among them, suggesting that they tended to compete with each other. Consequently, some regulations tend to overlap each other and raise confusion for the local government officials. This situation has been triggered by attempts at administrative domination by each ministry, because the ministries are headed by ministers with varying backgrounds and political loyalties. Regarding oversight bodies, most of the local government officials perceive that their work is more organised and that the separation of responsibilities tends to be distinctive. From the five oversight bodies identified by the local government officials, two oversight bodies are perceived to have a great impact on the way local government officers undertake their work. These oversight bodies are the BPK and the KPK. The third party is the stakeholders, who have their own agendas, which they try their utmost to pursue.

These external parties affect the internal elements of local government in many ways, particularly in the procurement stages, including planning, selection of contractors, acquiring assets, and monitoring of the procurement stages. In the planning stage, several issues have been highlighted, which are detailed as follows:

- the dominant roles of heads of local government agencies,
- the implementation of new regulations alongside software application issued by each ministry,
- receiving assets from related ministries,
- the importance of competent and qualified staff to deal with the procurement process,
- engagement with local society and local parliament, and
- availability of an infrastructure database.

After the planning has been approved by the local parliament, the local government selects suppliers or contractors in a variety of ways, depending on the value of assets. The selection process will be handled either by the ULP or by an official from a local government agency. However, the selection of suppliers or contractors poses problems, specifically in terms of the availability of a database of blacklisted suppliers and a detrimental lack of involvement by professional bodies in dealing with this issue. Finally, after a supplier or contractor has been selected, the project is executed. The procurement of infrastructure in construction is a more complicated process than the procurement of equipment, because planning consultants, contractors and supervising consultants are involved. Therefore, this type of procurement becomes the main focus of attention for both formal and informal bodies, i.e. the inspectorate, the BPKP, the BPK, NGOs, local society, mass media, the district attorney and police officers with various (not always legal) interests as well.

In the next chapter, patterns of the interaction of external parties with elements of local government are depicted with reference to the historical development of local government administration, which is framed from a Foucauldian perspective.

Chapter 7

Connecting Theory, Values and Practices

7.1. Introduction

This study has been conducted within the context of bureaucratic reforms that delegate more authority to the local government level, and the intention of the central government to establish mechanisms of financial control, particularly on capital expenditure. The findings of this study indicate the involvement of many parties affecting the control mechanisms of capital expenditure at various levels, which influence the dynamics of local government organisation. Indonesia's local governments intend to provide infrastructure in order to stimulate economic improvement within the local government. Therefore, this proportion of the capital

expenditure has been increased and become the second largest allocation after the routine spending. As capital expenditure involves vast sums of money, it attracts many parties to get involved in the capital expenditure processes alongside their various interests. Every party tries to exercise their power in the processes, which puts more pressures on local government officials.

Within this study, mechanisms of capital expenditure control have been investigated, not only as a discourse, but as real practices alongside the real impact they have, particularly on the involvement of many parties and the power relations among those parties. This study employs a Foucauldian perspective as the method of investigation, as this perspective focuses on approaches to the governance of self and others. In addition, this study is related to a government institution that is very sensitive to laws and regulations; this study therefore applies updated regulations and laws as references. An extensive study on laws and regulations in this study is conducted and considered as secondary data to support the primary data.

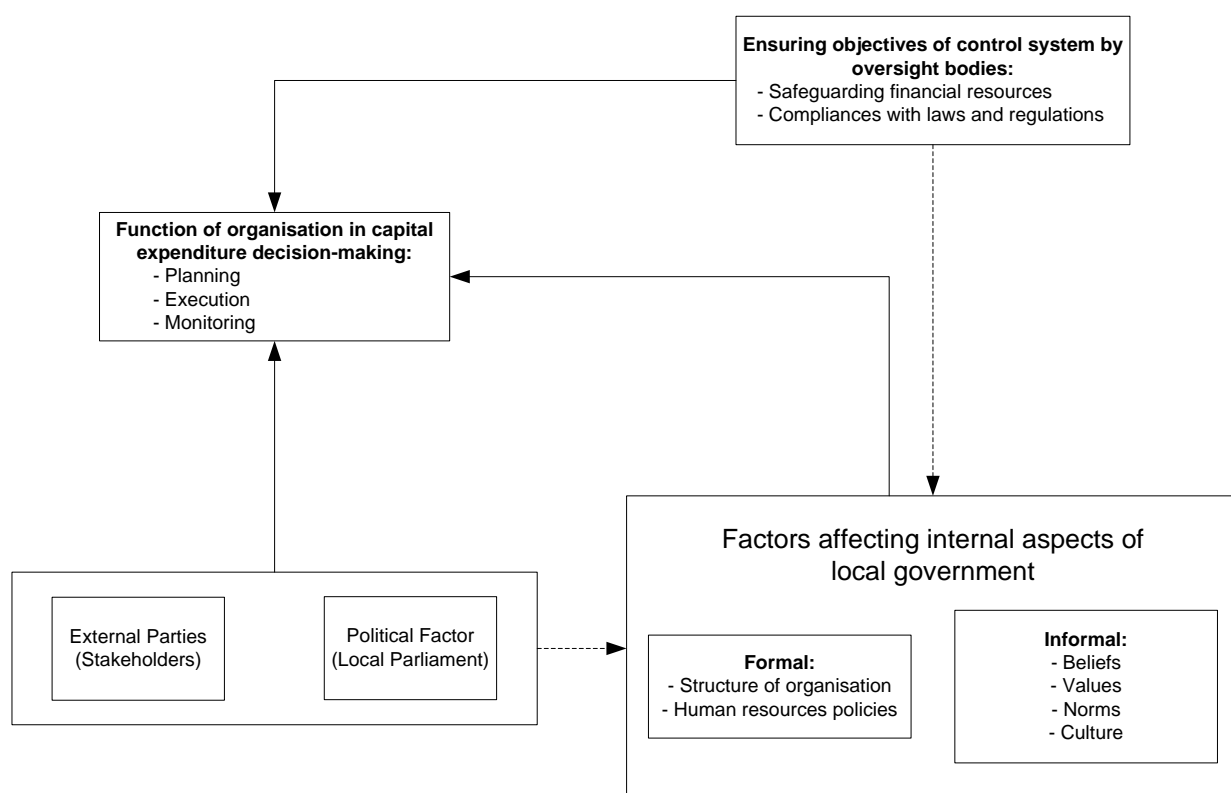
This chapter contextualises current practices of mechanisms of capital expenditure control in sampled local government areas, which is reflected in the data produced, along with interpretations of the findings based on a Foucauldian perspective and historical views on the practices.

7.2. Impact of Each Party on Capital Expenditure Control

Power relationships within organisations are regarded as very complex in nature and there are no specific tools for studying them. However, Foucault suggested that there are two models of power: legal or legitimate power, and the institutional model. Furthermore, regarding the analytical work of the power relation, Foucault suggested considering conceptualisation of particular objectification. The conceptualisation encompasses critical thought and constant review of phenomena of objectification based on historical conditions and current reality. Hence, conceptualisation becomes the main basis of analytical work (Foucault, 1994, p.327). Another alternative approach to investigating power relationships is suggested by Foucault, and is regarded to be a more empirical method, more reflective of current conditions; it uses analysis of the form of resistance as a starting point. The resistance is used to identify the position of a particular party and the methods being used

(Foucault, 1994, p.329). Therefore, the following figure depicts the interrelationship among parties and the power exercised among those parties, together with the impact of those aspects on functions of capital expenditure control of local government. Moreover, historical conditions are also considered in order to give insight into the current conditions.

Figure 7.1. Interrelationships of the many aspects affecting the capital expenditure control



Source: Original

This figure illustrates the roles of several parties in capital expenditure control of local government, including the oversight bodies that both directly and indirectly affect the process by influencing internal aspects of local government. Likewise, the stakeholders and political factors also exert direct and indirect influence. Meanwhile, the internal factors of local government, which are shaped formally by the laws and regulations imposed by central government bodies and informally by pressure from local stakeholders and political factors, affect the implementation of capital expenditure decisions. The internal factors comprise formal aspects, including the structure of an organisation and the human resources policies in place within that organisation. Also involved in the decision-making process are informal factors, such as beliefs, values, norms and culture. Further elaboration of the interrelationships of all these components, as presented in the figure above, is contained in the following sections.

7.3. Achieving the Objectives of the Control Systems

Establishing control systems in Indonesian local government is started by issuing laws and regulations, some of which need to be further elaborated on by presidential or ministerial decree. These control systems involve three main parties: (i) ministries, as the representation of central government; (ii) the BPK, in its role as external auditor of the central government; and (iii) the BPKP acting as the internal auditor of central government. The laws and regulations are implemented in local government areas, and the local governments need to adhere to these in an attempt to safeguard financial resources and to control and prevent corruption. Thereafter, the laws and regulations become points of reference from which the auditors undertake their assignments, and they must be regularly reviewed and revised in accordance with the dynamics of government organisation. Thus, the imposition of moral values, stricter methods of surveillance and more efficient techniques for gathering information are also developed in order to eliminate corruption and fraud. As modus operandi of illegal practices will develop continually and involving more complex mechanism (Foucault, 1977); hence, the methods and techniques need to be reviewed and developed continually as well.

Engagement of those parties in the capital expenditure of local government impacts the local government, both in formal ways, such as organisational structure and human resources policies, and informal ways, linked to the beliefs, values, norms and culture within the local government organisation. One of the formal aspects affected is organisational structure, which is exemplified by the establishment of a special unit to provide procurement services in accordance with Presidential Decree 106/2007; however, the level and quality of implementation of the decree varies across the sampled regions. The establishment of the ULP has been endorsed in order to improve the transparency of procurement processes, as the ULP involves cross-functional officers from local government agencies. This approach can be perceived as an attempt by central government to adjust mechanisms of power through adaptation and refinement of the local government body, which is initially fully responsible for the procurement of fixed assets, by establishing a special unit. The special unit is placed under surveillance so that everyday behaviour, identity, activity, and policy can be monitored by the head of local government at the local government level, and by the LKPP in central government level (Foucault, 1977). This idea places emphasis on hierarchical surveillance, as in a military camp in which the layout, number of tents and

direction of tents are all precisely mapped, enabling superiors to exercise their power (Macintosh, 2002).

The Indonesian local government has adopted the idea of hierarchical authority, especially in the establishment of the ULP as a special unit for procurement, which is intended to be the sole method of procurement and to enable local governments to optimise their procurement processes, particularly for high-value procurement. Thus, the head of local government and heads of local government agencies can monitor the processes of capital expenditure through this unit. Several heads of local government agencies chose to hand over their agency procurements to the ULP rather than be audited by the BPK. The BPK is regarded as a highly influential and powerful institution that could, under certain circumstances, endanger an official's future career. It is therefore better to avoid it than to confront it. In addition, the involvement of cross-functional officers from many local government agencies is expected to strengthen the ULP, as each section is occupied by the highest quality officer from each local government agency. The highest quality of officials for the ULP is necessary, as this unit encounters many pressures from many parties. However, although the establishment of the ULP has been endorsed since 2007, the implementation of this unit is still in the early stages because of a lack of qualified officers to handle procurement processes.

The second formal aspect of local government decision-making is the issue of human resources policies. Of particular relevance are the moratorium on local government officials, the complexity of and difficulties related to the dismissal of government officials, and the long-established emphasis on seniority instead of meritocracy. These examples pose diverse problems for local governments. In order to deal with these human resources policy issues, it is suggested that an institution employing a supervisory hierarchy should adopt normalising sanctions, such as those that are or were employed in schools, military establishments, prisons, hospitals, factories, and other state bureaucracies (Macintosh, 1994, p.226). Furthermore, Macintosh (1994) suggested that sanctions are designed to motivate officers in order to achieve higher levels of competence and to reduce the gap between norms and actual behaviour. Regarding human resources policies, the central government needs to give more attention to sanctions and penalties that can be used to normalise the behaviour of local government agencies. For example, current policies are insufficient when it comes to the issue of dismissing a government official. It is very difficult to dismiss a

government official unless he/she has been convicted, with severe punishment, in a court of law. Any violation of rules will only be punished leniently by local government agencies, each of which will apply different policies on sanctions based on the discretion of the head of the local government agency or the head of local government. This leniency of punishment is highly influenced by local culture, which tends to avoid confrontation, especially with senior officers.

The most common approach to establishing a relationship and exercising power by superiors over subordinates is through formal ceremonial behaviour, known as *apel*, which is used to convey any messages or instructions from a superior to his or her subordinates. This practice originated in the 19th century, when it was used by government officers (called *priyayi*) and was known as *seba*. This practice was intended to show the devotion of government officials to the monarch. It signified the availability of the *priyayi* to serve and receive any instructions from the monarch or a superior. Moreover, it also had the political dimension of showing submission towards authority and the rule of superiors, thus emphasising the formal relationship between subordinate and superior (Moertono, 2009).

To date, the *seba* practice is still preserved in government offices, which can be perceived as helping to maintain and affirm the importance of formal relationships. It is reasonable to conclude that Indonesia still has a significant power imbalance between superiors and subordinates (Hofstede, 1994). This relationship puts the leader at the centre of an organisation, as confirmed by many interviewees; thus, development in an organisation depends heavily on the position of the leader. This situation sees the leader, or superiors in general, as immune from criticism from subordinates, as expressed in a common joke: '*Rule number 1, superior never makes a mistake; rule number 2, if superior made a mistake, please refer to rule number 1*'. This joke cynically renders anyone in a lower position subject to, and subjected to, the 'perfect and faultless' individual in the higher position.

Apart from formal and observable impacts, imposing laws and regulations also impacts a local government's beliefs, values, norms and culture. An example of this is the drive to improve transparency and disclosure of information to the public, as required in law 14/2008. This law requires government officials to deal with many stakeholders who are interested in particular pieces of information; a practice that has never been done before. Hence, in order to understand an institution from a

Foucauldian perspective, one must not only relate to its legal formal character, but also become involved in its composition of government officials and the patterns of behaviours associated with it (Bevir, 1999). The institution can be understood by the ideas or concepts that characterise it. Furthermore, Bevir (1999) exemplifies this notion using the character of a state, which can be understood from its ideas of sovereignty, discipline and pastorship. Likewise, the concept of pastorship can be grasped from values, ideas and practices developed within the Christian church (Bevir, 1999, p.352).

Referring to the findings of this study from the perspective of pastorship, local government officials, as governed individuals, can be regarded as members of a flock who need to be led along, with certain rights attached to them (Burchell, 1991). Furthermore, he described this as “children to be corrected and educated, as part of a natural resource to be exploited, or as living beings who are part of a biological population to be managed” (Burchell, 1991, p.120). In this concept, the local government official, as an individual, is required to internalise various values and norms that are contained in the laws and regulations of various oversight bodies as external entities. In this case, the central government bodies must be able to impose and internalise new values concerning transparency that make it much more prudent for local government officials to execute procurement decisions in order to comply with all laws and regulations; otherwise, the local government official will face sanctions for deviation from those laws and regulations. Since the local government officials are concerned with their own wellbeing, they strive to regulate themselves in accordance with the dictates of that external body by scrutinising their own behaviour for signs of ‘sin’ or abnormality, as defined by the powers that be (Bevir, 1999, pp.349-350). This condition shows that, because they holding the power, the central government bodies see the local governments as ‘subjects’, which can be defined in two ways: (i) as being subject to another party through control and dependency; and (ii) as being subject because of consciousness of identity or self-knowledge. The subjectification can be studied based on mechanisms of exploitation and domination among related parties (Foucault, 1994, pp.331-332).

The subjectification of local government is settled when the central government issues regulation regarding fiscal balance (UU 33/2004), which emphasises the implementation of fiscal balance mechanisms through DBH (*Dana Bagi Hasil* / Revenue sharing), DAU (*Dana Alokasi Umum* / Generally allocated fund), and DAK

(*DanaAlokasi Khusus* / Specifically allocated fund). Through these mechanisms, local government has a fairly strong dependence on central government. Particularly, since capital expenditure is mostly funded by the DAK; hence, engagement with central government via related ministries for decisions of capital expenditure is immense. Any decisions regarding capital expenditure must be in line with the priorities of the related ministry.

From Foucault's perspective, the role of oversight bodies can be identified as being that of 'police'. Historical definitions of police are different from a current or contemporary definition (Foucault, 2007). In the sixteenth century, 'police' was defined as an agency that serves the splendour of the entire state and the happiness of all its citizens. The agency used a set of laws and regulations to establish and strengthen the power of the state (Foucault 2007, p.314). In Indonesia today, the 'police' concept relates to the roles of two oversight bodies: the BPK, acting as the government's external auditor, and the BPKP, acting as the government's internal auditor. In addition, the KPK comes onto the scene as a new and powerful institution designed to deal with, control and eradicate collusion and corruption. In its role as internal auditor, the BPKP engages intensively with local government officials to give input regarding compliance with laws and regulations. Although they build good trusting relationships with local government officials, the BPKP officials are rotated regularly in order to avoid the possibility of collusion with those local government officials. Similarly, the BPK officers, as external auditors, are rotated even more often than the BPKP officers. The BPK is responsible for auditing the implementation of capital expenditure and recording all transactions according to government accounting standards. From their records the BPK later produce audit opinions regarding the validity and fairness of the financial statements of local governments. As well as a standard financial audit, if necessary the BPK might also conduct a forensic audit. In addition, if the BPK audit finds any irregularities in a project's procurement, the BPK can hand the details over to the KPK, the anti-corruption committee. The KPK will then investigate further and formally undertake prosecution in the anti- corruption court.

Moreover, attempts to control the behaviour of local government officials are also undertaken by related ministries in the form of implementing the application of planning software when dealing with capital expenditure. From a Foucauldian point of view, such attempts can be regarded as applications of disciplinary power based on a panopticon model, which is described as a constant surveillance system (Foucault,

1977). The main intent behind this method is to define, control and regulate individuals who are subjects of regimes of power (Bevir, 1999, p.352). The implementation of mechanisms of control of capital expenditure, through the employment of a particular software application as a device of a related overseeing ministry, can be perceived as an imposition of disciplinary power. The assets that are to be procured have been pre-determined by the relevant ministry along with all requirements related to supporting documentation without consideration on the local government agency's needs.

Macintosh (2002) divide the concept of disciplinary power into three aspects: disciplinary space, disciplinary time, and disciplinary body. The first aspect of disciplinary power is 'disciplinary space', which the software application provides by determining allocations and ensuring that any proposals other than those specified will not be accommodated. The specific allocation will enable the ministry to manage capital expenditure. Hence, it allows identifying the total budget, which is aimed to meet specified targets for budget spending. Meanwhile, from the local government agency side, this practice will ensure a source of funding for a particular area of capital expenditure. The second aspect of disciplinary power is 'disciplinary time', which requires each local government agency to set out a time frame of implementation of capital expenditure, enabling each concerned ministry to monitor the progress of local government agencies. On the other side, a local government agency is induced to adhere to a time target, which compels the local government officials to act effectively and efficiently. The third aspect of disciplinary power is 'disciplinary bodies', which enable the monitoring, sanctioning and examination of a particular local government agency by a related ministry or ministries. Implementation of capital expenditure is monitored by the related ministry, which can impose sanctions if it finds any irregularities. If the related ministry suspects a potential irregularity, the ministry will send a team to scrutinise the issue before involving any other bodies, such as the BPKP and the BPK. All of these aspects of disciplinary power reflect Bentham's panopticon mechanism: the tower in the centre of Bentham's prison building enabled a warden to monitor all cells around the tower. In this analogy, the tower is the software application implemented by a ministry that enables the monitoring of every cell; that is, the monitoring of local government agencies from the capital city. By employing this practice, local government agencies can be constantly monitored by their related ministry or ministries.

7.4. Influence of Stakeholders and Political Power on Capital Expenditure

7.4.1. Influence of Stakeholders

The social forces or stakeholders, represented by the engagement of local society, non-government organisations (NGOs) and professional bodies, affect practices in local government in two ways: the implementation of the capital expenditure process and influencing the internal dynamics of local government. The idea of the empowerment of stakeholders in this era can be justified from the viewpoint that a person or an institution will not be able to encompass all aspects and that many areas will be neglected (Foucault, 1994, p.74). This notion suggests that the human resources of the oversight bodies are very limited when compared to the number of local governments to be overseen and the numbers of regions in which they are located, scattered over many islands. Therefore, empowering stakeholders is an alternative means of strengthening control over local governments. The formal forces are expected to give information to oversight bodies that can be followed up by further investigation if any suspicion of irregularities in procurement processes is found.

However, the influence of local society as the main stakeholder is still low, and any involvement is regarded by local government officers as an attempt to comply with regulations regarding the involvement of local society in the planning stage of local budget setting. The local government bodies have the power to impose their plans on the local community, giving little consideration to the needs of local society. This practice is in line with what was suggested by Foucault (1994): that discursive practices are not only related to producing a discourse, but also to imposing and maintaining that discourse in a form of technical ensembles, institutions, behavioural schemes, types of transmission and dissemination (Foucault 1994, p.12). Referring to this notion, discourse about the requirement of involvement of local society in planning stage is facilitated by local government through a formal gathering, i.e. Musrenbang (*Musyawarah Perencanaan Pembangunan* / Development planning meeting) or Jaring Asmara (*Penjaringan Aspirasi Masyarakat* / Collecting public aspirations/opinions). In this case, a local government used the involvement of local society in the planning process as a discourse, which was followed by a technical ensemble in the form of Musrenbang or Jaring Asmara involving local society, political parties and other interested elements. In this event, the local government communicated both their short- and long-term plans to local society instead of gathering and meeting local society's

needs. By holding this event, the local government will be able to claim that local society was involved in the planning process, as required by regulation.

Actually this practice can be traced back to the seventeenth century, when Javanese society was divided into three classes. The upper class comprised the king and noblemen; the middle class was *abdi dalem* (the king's servants as the lower middle class) and *priyayi* (the king's officials as the upper middle class); and the lowest class was the common people (Moedjanto, 1990; Moertono, 2009). These classes are still preserved, especially in the relationships between government officials, previously represented by the *priyayi* class, with the public as the 'common people'. Traditional perspectives suggest an absence of reciprocal obligation between superior and subordinate: "Any such system would have had to admit a formal reciprocity in political relationships, fundamentally alien to Javanese thinking" (Anderson, 1990). Therefore, the higher class (*priyayi* or government official) might impose obligations on the common people.

The other stakeholder is NGOs, organisations that flourished after the reformation era. The NGOs affect capital expenditure processes, particularly in the setting of local budgets, together with other local societies. Moreover, the NGOs also become involved in monitoring particular projects that indirectly exert another source of pressure on local government officials. This pressure can be seen as highly constructive if it convinces the official to adopt a new set of values in order to become more accountable and transparent. In this context, the local government encounters different elements of society, and therefore applies different approaches. Foucault (1994) suggested that the transformation of discursive practices is affected in three ways: outside the discourse, reflected in the form of relationships with social and political institutions; within the discourse, such as techniques applied in order to determine object, refinement and adjustment of concepts; and alongside the discourse, by producing other discursive practices (Foucault 1994, p.12). Since Indonesia's reformation era, there has been a discourse raised regarding strengthening the roles of local society through involvement in government decision-making. The NGOs in particular are an important element of society. Engagement of local governments with NGOs is quite intense, requiring local government officials to find good ways of dealing with them, as each NGO has a different agenda. Some NGOs truly engage with local governments in the interests of local society and communities; but a few NGOs have agendas in place for their own good. This pressure situation is exemplified the

case of a NGO intimidating a local government by threatening to expose an alleged irregularity in a project if the particular local government agency did not provide some money to the NGO. This is powerful leverage, because if a case is exposed via mass media and gains public attention the local government agency has to make itself accessible to many concerned parties, including the BPK and the local attorney. Dealing with NGOs tends to be more complex than engaging with local society, as the NGOs have more knowledge related to public expenditure and government procedures than local society. Hence, different approaches are necessary when dealing with these two groups.

Another stakeholder is professional bodies that are required to regulate their members in accordance with laws, regulations, customs and codes of ethics. However, the roles of professional bodies are still low in terms of importance and effectiveness, and they do not meet the expectations of local government officials in terms of regulating their members. This situation can occur as the result of lacking a system of communication as a means of exercising power; power that is supposed to be held by the professional bodies therefore cannot be exercised over its members (Foucault 1994, p.17). When local government officials are dealing with the issue of an unreliable contractor, they perceive that the professional body does not have any power to control their member. After a case occurred in one area, the unreliable contractor is still free to participate in procurement in other regions. An integrated database is not available at a provincial level, but rather communication is conducted personally among local government officials. Thus, attempts to restrict the movement of the unreliable contractor are still limited in their effectiveness.

Involvement of social elements, which are represented by local society, NGOs and professional bodies, not only affects the social values of local government, but also impacts the structural organisation of local governments and their human resources policies. Consequently, the structure of the organisation in each local government is not the same. This variation exists in order to accommodate the dynamics within each local government, which are very different, especially between rural and urban regions. For example, the city of Yogyakarta established an agency, the DGBAD (*Dinas Gedung, Bangunan, dan Aset Daerah*), that is responsible for managing the fixed assets of the local government. This agency was established initially as a response to input from local society regarding many assets of the local government that had not been identified and recognised in its financial statements. This type of agency cannot be found in any

other local government in Indonesia. The influence of local society on human resources policies is reflected in the initiatives of local governments to gather input from local society regarding any service provided by a particular local government official or an agency. The local government provides forms, both online and via paper, to allow local society to assess the services that have been received. In some cases the assessment of local society may affect the performance evaluation of an official, but there is no sanction imposed relating to that feedback.

7.4.2. Influence of Political Power

Another issue relates to the role of political power, represented by the local parliament, in which the members are from various parties and are elected directly by local society. In this context, basic decisions of the members of parliament are affected by several things, such as (i) by their party, for each party has its own agenda that must be enforced by its members. In addition, (ii) local society, as constituents of the MPs, should be accommodated in order to get their support. Finally, (iii) the members' interests dictate that each member of parliament has a duty of reciprocity to his/her political party in terms of financial support for that party. Referring to these conditions, the members of parliament will have a tendency to exert his/her authority on local governments in order to achieve his/her interests. Particularly in local budget setting, local government officials feel more pressure, and those officials need to be able to manage and deal with the many interests of the local parliament's members. In particular, the setting of the local budget on capital expenditure is more complicated than other allocations in local budgets. As such, execution of capital expenditure needs more time than any other allocation, beginning with the selection of suppliers or vendors, execution of the procurement, and handing over the asset or assets to a particular local government agency.

Interaction with the local parliament does not structurally affect a local government organisation, but it influences the behaviour of local government officials. Particularly in budget setting, it leads to various reactions, especially when a local government is dealing with capital expenditures that are allocated from amendments to the local budget. Those reactions are exemplified by certain officers, such as a government official finding a risky method, which does not comply with the legislated procedure, in order to meet the local government agency's budget spending target. Meanwhile, other local government officials avoid executing the procurement of any

assets, as time is regarded as being very limited, making the situation too risky to violate the regulations. In consequence, these local government agencies could not meet their set budget spending targets.

The “New Order” regime has been ruling for more than 30 years over all areas of Indonesia, and it has undermined the position of parliament at both a national and sub-national level. Under this regime, the position of parliament, either at a local or sub-national level, can be regarded as merely an ornament of democracy, powerless compared to the executive body. The momentum of reformation has reinstated these parliaments, along with their power as legislative institutions. Now the local parliament is able to exercise its power as a legislative body over a local government agency as an executive body. On the other side, local government officials reacted to the objectification attempts in various ways, as described above, even if that meant taking risks. From a Foucauldian perspective, this phenomenon can be understood by referring to two ways of logical thinking about power, one based on a legal model and one on an institutional model. The local parliament in this case has a power base informed by both models. The legal model posits that the members’ positions have been legally recognised as legislative bodies referring to laws, while the institutional model recognises that they get formal support from local society in direct elections. Therefore, the position of the local parliament is considered to be very strong and becomes a counterpart to the head of local government, who is also appointed through direct election. However, as the positions of the local parliament and the head of local government are equal, the local parliament therefore cannot dismiss the head of local government.

The tendency to exercise power over lower level officers can be traced back to practices in the early 19th century, which were observed by Raffles (2015). If the Javanese was a person of rank, he tended to be very proud and slavish towards his superiors. Meanwhile, toward his inferiors he would be mean, arrogant and despotic (Raffles, 2015, p.276). Foucault suggested three modes of objectification that transform human beings into subjects. The first mode is that people try to give themselves a particular status; the second mode is called “dividing practices”, in which the subject is either divided within himself or divided from others; and the final mode is that he turns himself into a subject (Foucault, 1994, p.326-327). Referring to Raffles’ observation and modes of objectification, the local parliament applies the second mode, dividing practices between “superior” and “subordinate”, although structurally there is no direct

link of responsibility between the local parliament and local government agencies. Raffles observed that Javanese people tended to be sensitive to praise or shame, and were ambitious in pursuing power and distinction. Furthermore, in Javanese culture it was necessary for individuals to distinguish themselves as members of the privileged classes of society, and as therefore “different” from the common people. Suffering from long oppression has injured the bright character of the common people, while the privileged class tend to constantly exercise an absolute dominion that is sometimes expressed in violence, deceit and gross sensuality. Thus, in Javanese society, power can be clearly felt and seen; rank, wealth and authority can be identified easily, and different classes are noticeable (Raffles, 2015, p.287-288). Today, the observations of Raffles are still relevant in understanding the inclination of the local parliament to exercise its power over local government agencies.

7.5. Impact of Improvement of Internal Factors on Capital Expenditure Practices

There are two main aspects to the impact of the interrelationships of various parties on internal factors: the formal aspect that concerns organisational structure and human resources policies, and the informal aspect that focus on beliefs, values, norms and culture. In this section, the discussion emphasises the informal aspect, as the formal aspect was discussed in the previous section in relation to formal bodies of central government. The influence of central government bodies is reflected in engagement of ministries and oversight bodies with local government. In addition, the local society’s power over local government is signified by political forces that are reflected in local parliament, while social power is embodied by stakeholders consisting of local society, NGOs and professional bodies. The influence of those factors on organisational beliefs, values, norms and culture can be identified by determining the differences between initial values and the current values applied by the local government officials.

Raffles (2015), in his book *The History of Java*, depicts the conditions and character of local society, particularly Javanese society. In his observations, Raffles characterises the Javanese as having a despotic government, upholding feudalistic principles and being a patriarchal society. The government based on feudalistic principles tends to disregard the common people, and some local aristocrats even considered the common people living in their areas as their slaves (Raffles, 2015). Currently, this over 200 year old phenomenon is being eroded by involving local

society in the process of local budget setting, although the engagement is still superficial. Regarding Java's patriarchal society, Javanese tend to rely on the ruler (Pigeaud, 1967) "in Javanese culture rulers and noblemen occupied an important place in the centre of human society, and so their behaviour was a model for all" (Pigeaud, 1967, p.72). This characteristic of society is still preserved in local government practices, in which local government agencies rely heavily on the roles of heads of agencies. However, this characteristic tends to diminish in urban regions, where local government officers work more independently than officers in rural areas.

7.6. Summary

This study focuses on control of capital expenditure in Indonesian local government. It is an interesting subject of study, as it involves a vast amount of money attracting many parties to participate in the decision-making process of capital expenditure. This study has identified the parties involved, and also how those parties affect local government, either formally or informally. Furthermore, this study has also identified the discourses instigated by each party that affect the control of capital expenditure. Thus, in order to understand those discourses, this study applies Foucauldian perspectives to the interactions among parties in terms of how those discourses affect control systems, formal structure, procedures and organisational values.

The main issue found in this study is that the capital expenditure control of local government still needs to be addressed. The involvement of oversight bodies imposing laws and regulations has affected local government directly and indirectly. The direct effect is on the phases of capital expenditure, while the indirect effect is influence through the internal aspects of local government that encompass organisational structure, procedures and values, which later affect capital expenditure processes. The oversight bodies structurally related and have power to impose its power to local government. Local government officials must follow all instructions from those bodies in order to adhere to regulations, although there have been some cases of resistance towards the imposed power.

In addition, this study also indicates the importance of stakeholders and political power in the form of the local parliament. Likewise, these parties also affect the capital expenditure process in local government, both directly and indirectly. The local parliament, as representation of political power, is legally able to exert its power

over local government, although structurally the local parliament has no relation to the local government. However, the local parliament is a legislative body and a counterpart of local government, that acts as an executive body. Therefore, the local government must comply with the local ordinances that are ratified by local parliament. Another party is the stakeholders, which encompasses several parties; specifically local society, NGOs and professional bodies. Although involvement of this party institutionally has been accommodated by regulations, the local government tends to disregard its role. The local government's treatment of the stakeholders can be understood culturally, which engagement of the common people used to be neglected.

Referring to those indications, the local government tends to adhere to power based on a legal model rather than an institutional model. The power based on a legal model is held by central government institutions, such as ministries and oversight bodies, and local institutions, such as the local parliament. Meanwhile, the institutional model is signified by the involvement of stakeholders. Thus, the implementation of an capital expenditure control mechanisms tends to be more of an administrative matters, such as compliance to the requirements set out by the formal bodies, and neglecting the roles of the non-formal bodies to strengthen the mechanisms of capital expenditure control. The overall conclusion of this study is presented in the next chapter.

Chapter 8

Concluding Remarks

Indonesia experienced a severe financial crisis when the value of its currency plummeted as a result of the Asian financial crash in late 1997. Consequently, many companies collapsed and the country's financial sector was paralysed. In order to eliminate the negative effects of this crisis, the GoI invited international institutions, represented by the IMF, to intervene in order to restore the nation to something like pre-crash conditions. However, as a condition of the involvement of the IMF, the GoI had to sign several LoIs that must be implemented by the GoI. The LoIs embraced reformation in many aspects, but their key purpose was to encourage enhancing

transparency and accountability in the GoI, as previously Indonesia had been ruled with an authoritarian style of leadership, which was opaque and unaccountable.

One of the LoI's programmes was decentralisation, which required the central government to devolve its authority to local governments. As a result, nowadays local governments manage more power and resources than ever before; even capital expenditure decisions are now authorised and managed by the local government itself. In order to accommodate this situation, and to eliminate the possibility of financial irregularities, the GoI set control mechanisms by issuing regulations and empowering other parties to strengthen the controls.

The objectives of this study are therefore as follows: first, to describe the setting of control mechanisms of capital expenditure, and the influence of the new mechanisms on practices at local government level; second, to identify the engagement of any other parties and the impact of that engagement on established control mechanisms; and finally, to explore local government officials' perceptions of the involvement of such parties. This study applies a Foucauldian perspective to analysing those changes and the interaction of these parties in attempts to strengthen control mechanisms of capital expenditure.

Referring to those objectives, this study encompasses several aspects of the implementation of new financial control mechanisms in Indonesia's local governments. The discussion begins at a time of intervention by international institutions, following the 1997 financial crisis, in an attempt to establish good governance. The intervention of international institutions not only involved funding, but also introduced new systems that had to be implemented by the GoI. The findings of this study indicate that introducing a new system into an organisation can trigger resistance from organisation members, including members of local governments. Particularly in Indonesia, where the culture of government offices and officers is influenced by traditional and long-standing aristocratic values, those government officials are perceived to be of higher status than ordinary people. The government tends to be a closed organisation which is not transparent to members of the public, who are regarded as commoners. Hence, introducing a new system that emphasises a culture of transparency and accountability has created high levels of resistance from civil servants, because the new system contradicts the old aristocratic culture that had been in place for decades.

In an attempt to deal with this problem, the central government intends to involve professionals from the private sector who are perceived as being familiar with a transparent and accountable culture at ministerial level. However, this move cannot be implemented within the lower levels of personnel, because the government's staffing system relies on seniority and prohibits hiring professionals (i.e. outsiders) for key positions, such as for heads of local government agencies. Consequently, many programmes that have been designed cannot be implemented as intended. All procedures are applied only as formalities in order to meet the pre-determined requirements; for example, the implementation of standard operating procedures (SOP) in every local government agency is applied based on the discretion of the head of that particular local government agency.

The main ministries have set up many programmes by issuing regulations in order to strengthen control mechanisms, although sometimes such actions raise confusion for local government officials because of overlapping, contradictions and redundancies contained in the issued regulations. The confusion tends to increase in particular for local government agencies that are placed under several ministries in charge of a particular field or area. Another issue related to ministries emerge when a particular ministry allocates equipment or other fixed assets to a local government agency even though the agency sometimes does not actually need that asset. Just as problematic is when the allocation is not accompanied by an official letter handing over the equipment to the local agency; the equipment cannot therefore be recognised as an asset of the local agency and thus procedurally it cannot be maintained from the local government's budget. Meanwhile, the equipment requires maintenance, but the related ministry does not provide funds for this. The outcome of this is that the equipment will not be used, is used until it breaks, or is maintained using other sources of funding, meaning that the agency will mark up another account in order to be able to maintain the asset from the local budget.

Local government acquires assets is not solely rely on the grant from related ministry, but the local government can procure its own asset. Regarding the procurement, the GoI has recently implemented a system of e-procurement in order to eliminate the occurrence of irregularities in procurement processes. E-procurement requires the establishment of a new organisational unit, known as the procurement services unit or ULP. All procurements above IDR 200 million will go through this unit and will no longer be handled by local government agencies. However, this method has

not worked as well as expected for several reasons. First, members of the ULP must be certified as procurers, and local governments, particularly in rural areas, are still lacking qualified human resources. Second, the ULP can still be subjected to intervention by the head of a local agency in favour of one of the tender participants, for example. Third, there is a lack of an integrated database of suppliers, which enables blacklisted suppliers from one region to participate in tendering in other regions. Finally, local government agencies have a tendency to break down a procurement that is initially worth more than IDR200 million into several smaller procurements, thus allowing the process to be managed by the local agency.

Apart from the internal aspects of government, the involvement of other elements is required to strengthen the control mechanisms that have been established by central government ministries. The first element is oversight bodies, which are regarded as important for controlling capital expenditure. However, local government officials tend to give more attention to those bodies that threaten severe punishments if they find financial irregularities, i.e. the BPK and KPK. Second, the stakeholders in local governments have not been involved as required, although the condition of their involvement is underscored in the LoI from the IMF. This can be seen in the involvement of local society in *Musrenbang* as a way to legalise a predetermined work plan. On the other side, all of the identified stakeholders have own agendas and try to realise it. Overall, the control mechanisms of capital expenditure in local governments can be perceived as being still vulnerable to irregularities committed by local government officials.

A Foucauldian perspective has been employed as an analytical lens in this study in order to create a framework for identifying the positions of interrelated parties and how power in each party is exercised over the others during decision-making regarding capital expenditure at the local government level. The Foucauldian perspective is fitting for this study, as it offers historical and cultural reference points when portraying the current situation. Hence, these approaches have been implemented in this study in order to obtain a basic idea of the current practices existing in Indonesia in both central and local government offices.

A culture of transparency and accountability that is endorsed by international institutions in governance reforms has changed the organisational structure substantially, which has affected the structure of power at both the central and local

governments level. Thus, employing a Foucauldian perspective in Indonesian local governments can be expected to reveal who holds power, how that power is exercised, and how to deal with the exercised power. Although Foucault derived his ideas from historical and cultural approaches to Western society, this study shows that this approach can also be usefully employed as an analytical lens for considering organisational issues in other global regions outside Europe. This approach can be applied in other parts of the world by considering the history and culture of any particular region.

This study illustrates three main points related to the dynamics of organisation, particularly local government the organisation; these are the involvement of many parties with different interests, the influences of those parties, and the response of the local government officials towards those influences. Thus, this study gives an understanding of the interrelationship between influential parties and the discourses that arise surrounding the capital expenditures of local government. However, this study only focuses solely on the perspectives of local government officials, which opens up an opportunity for future study to explore the perspectives of other parties that have been identified in this study. Interview with members of regulators, oversight bodies and stakeholders is suggested. Hence, a holistic view can be acquired by involving all of those parties.

This study can be useful as an initial reference point for future studies, as this study also encompasses various aspects of capital expenditure, both technical and cultural, which have not been explored in previous studies. Previous studies on local government's capital expenditure focus on factors affecting capital expenditure decision-making, such as the composition of local government finance. However, none of these explores the deeper aspects of capital expenditure decision-making and how local government officials deal with the many issues related to it, particularly regarding the control mechanisms of capital expenditure. Thus, this study fills the gap by providing insight into the interrelationships between local government officials and the related parties in control of capital expenditure, starting with planning, decision-making, execution and recognition as an asset of local government. However, the sample population of this study is entirely located on Java Island, near the country's capital city, where qualified personnel are relatively easy to contact compared to other regions in the outer islands. Therefore, further study should be undertaken for the outer islands, with an emphasis on considering how local government officials are dealing with the

new procedures, particularly concerning capital expenditure, along with any cultural aspects inhibiting the implementation of these procedures. The same approach and theoretical basis might be applied to the outer islands and hence the findings of a study in Java Island can be compared with findings from the outer islands.

This study also considers the influence of cultural aspects on the implementation of capital expenditure, and has found that the influence of organisational culture and the implementation of control mechanisms are highly related, as evident in rural areas where the role of the head of a local government agency is still dominant. His/her staff tends to be more passive and compliant compared to staff in regions surrounding or adjacent to provincial centres. Currently, the central government, through related ministries, is focusing on “hard control” by issuing and revising regulations and introducing new systems in order to establish rigorous procedures. However, the importance of “soft control”, which is needed to complement the hard control that has already been established, is still neglected. At the moment, “hard control” is more advanced than “soft control”, and the less attention given to “soft control” inevitably inhibits the implementation of hard control. Thus, this study prescribes importance to the balance between the implementation of soft and hard control systems in a government organisation.

In addition, this study contributes to current practice by sending an important message to Indonesian decision makers: that organisational culture, as well as procedural control in government offices, needs to be substantially reformed. For example, lack coordination among regulators that consequently affect the performance of local government officials because the officials have to prepare many administrative works to meet requirements of the regulators. Although the administrative works are intended to strengthen the control mechanism, it needs to be simplified without lowering quality of control. Hence, engagement of the oversight bodies also needs to be intensified that are not only emphasised on administrative works. Consequently, it requires more auditors as currently the number of auditors is not proportional to the number of local government as auditees. Regarding stakeholders, it still needs to be empowered and regulated, which their involvement is not only as an ornament to meet regulations but as components of control to support formal control undertaken by oversight bodies. Meanwhile, the internal condition of local government is necessary to get serious attention and needs to be reformed fundamentally, mainly upgrading the

quality of the local government officials and build egalitarian environment instead of stick on the patriarchal system.

In summary, the capital expenditure controls of Indonesian local government have been improving; however, in implementation the level of control varies depending on the conditions and organisational culture of a particular local government.

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APPENDICES

Appendix 1 Ratio of Capital Expenditures to Total Expenditures of Municipal Governments (in thousand IDR⁵)

YEARS	2006	2007	2008	2009	2010
Indirect Expenditure	87,405,357,099	108,548,513,241	134,527,570,742	156,617,007,328	188,589,276,241
Direct Expenditure	99,652,408,963	133,045,900,061	143,692,431,250	146,926,567,973	143,888,335,960

⁵ Exchange rate on 2006 – 2010, USD1 were between IDR9,020 – IDR8,991

TOTAL EXPENDITURES	187,057,766,062	241,594,413,302	278,220,001,992	303,543,575,301	332,477,612,201
Capital Expenditure	60,409,354,360	74,499,348,112	78,973,206,315	78,441,736,968	70,614,542,366
Ratio of Capital Expenditure to Total Expenditure	32.29%	30.84%	28.39%	25.84%	21.24%

Note: The table is produced based on data from Badan Pusat Statistik (BPS) / Centre Bureau of Statistic (www.bps.go.id).

Appendix 2

Ratio of Capital Expenditures to Total Expenditures of Provincial Governments (in thousand IDR)

YEARS	2005	2006	2007	2008	2009	2010
Indirect Expenditure	24,218,934,530	30,302,209,927	36,214,961,163	45,398,365,063	48,855,323,889	55,626,315,588
Direct Expenditure	24,980,872,207	34,483,611,934	39,726,141,320	43,212,462,677	53,029,301,998	58,446,922,847
TOTAL EXPENDITURES	49,199,806,737	64,785,821,861	75,941,102,483	88,610,827,740	101,884,625,887	114,073,238,435
Capital Expenditure	12,203,423,086	18,163,225,121	19,565,920,017	18,896,876,045	24,246,695,616	26,722,956,306
Ratio of Capital Expenditure to Total Expenditure	24.80%	28.04%	25.76%	21.33%	23.80%	23.02%

Note: The table is produced based on data from Badan Pusat Statistik (BPS) / Centre Bureau of Statistic (www.bps.go.id).

Appendix 3

Ratio of Capital Expenditures to Total Expenditures of Central Government (in thousand IDR)

YEARS	2007	2008	2009	2010	2011
TOTAL EXPENDITURES	504,623,000,000	693,356,000,000	628,812,000,000	697,406,000,000	908,243,000,000
Capital Expenditure	64,289,000,000	72,773,000,000	75,871,000,000	80,287,000,000	140,952,000,000
Ratio of Capital	12.74%	10.50%	12.07%	11.51%	15.52%

**Expenditure to Total
Expenditures**

***Note:** The table is produced based on data from Badan Pusat Statistik (BPS) / Centre
Bureau of Statistic (www.bps.go.id).*

Appendix 4
Development of Financial Control of Local Government

YEAR	SOCIO-POLITICAL CONDITIONS	LOCAL GOVERNMENT SYSTEMS	CONTROL FUNCTION IN LOCAL GOVERNMENT	FINANCIAL SYSTEMS	ACCOUNTING SYSTEM
1945 – 1948	Revolution still occurred, yet the Dutch did not recognise independence of Indonesia that adopted unitary state system.	The Indonesia central committee held an important position and became a legislative body in every region. Subsequently, the committee nominated governors for established provinces assisted by the ‘ <i>Badan Executive</i> ’ (Executive Body)	Head of local government led the legislative and executive body.	Bookkeeping referred to the Dutch regulations.	Cash basis and single entry
1948 – 1949		The local government had been divided into three levels in a hierarchical model. The government established local parliaments as legislative bodies along with local government councils as executive bodies at every level.	The head of local government held the position as head of the executive body, and as representative of the central government.		
1949 – 1950	As a part of formal recognition of independence, Indonesia must adopt a federal state system.	The Indonesian Republic became one of sixteen provinces/states, yet did not establish governmental system for a federal state.			
1950 – 1957	Indonesia already had formal recognition as an independent country. However, there were still many uprisings in many regions.	Indonesia re-established local governments at three levels in a hierarchical model. One improvement from the previous laws, that the head of local government was elected directly by the local parliament.	The central government took control over the local governments and abolished the role of the head of local government as the central government representative.	The government passed the law in 1955 concerning application of the cash basis in financial reporting.	
1957 – 1965	President ‘ <i>Sukarno</i> ’ declared ‘guided democracy’ which underplayed the role of parliament.	The government still divided regions into three levels in a hierarchical model. The local government consisted of local government councils and daily government agency. The role of local parliament was downplayed.	The heads of local governments gained position again as representatives of the central government, and the local parliament could		

			not demote the head of local government.		
1966 – 1998	The ‘ <i>Sukarno</i> ’ regime collapsed and was replaced by ‘ <i>Suharto</i> ’ regime.	The regions were divided into two levels of local government in hierarchical order. The local government consisted of local parliament as a legislative body, and the head of local government as an executive body. The head of local government was proposed by the local parliament, but the President had a prerogative to choose the head of local government that might be different with the proposal of the local government.	The head of local government again holds the position as government representative and must be responsible to the President. In addition, they also need to provide accountability reports to the local parliament.	In this era, government still applied the cash basis. The central government took control over financing of the local government budget.	
1999 – 2011	The ‘ <i>Suharto</i> ’ regime collapsed and the parliament adopted a democratic system, both for central and local government. The system also requires more transparent and accountable governmental finance.	The central government still applied the same zoning system; even more the government gave wide decentralised authority to the local governments to manage their revenues and expenditures. The local parliaments had broader authority than in the previous era. The local parliament could demote the head of local government. In this era, the government started to apply the direct election model, with people in particular areas voting for the head of their local government.	The heads of local government in districts and cities do not have hierarchical relation with the upper level (governor). However, they need to provide accountability reports to the local parliament.	In this era, the local governments have broader authority to manage their revenues and expenditures. However, they still relied on subsidies from the central government.	Applied cash towards accrual and double-entry system

Appendix 5

The Proportions of Fund Allocation from Central Government on 2012 to 2014

National Allocation	2012	2013	2014
<i>Dana Alokasi Umum (DAU)</i> (General Allocated Fund)	57.8%	59.8%	58.9%
<i>Dana Alokasi Khusus (DAK)</i> (Specific Allocated Fund)	5.5%	6.1%	5.7%
<i>Dana Bagi Hasil (DBH)</i> (Shared Revenue Fund)	21.8%	17.8%	18.5%
<i>Dana Penyesuaian</i> (Adjustment Fund)	12.3%	13.7%	14.1%
<i>Dana Otonomi Khusus</i> (Special Autonomy Fund)	2.5%	2.6%	2.8%

Source: <http://www.kemenkeu.go.id/Page/diagram-informasi-transfer-ke-daerah#node-4064>

Appendix 6

Previous Studies about Indonesian Local Government

Title	Studied by	Result
A case study of governmental accounting and budgeting reform at local authority in Indonesia: an institutionalist perspective	Djamhuri, A (2009)	Result of this study indicated that introducing of new budgeting and accounting system will cause decoupling due to the insufficient quantity and quality of staff in accounting and the rigidity of bureaucratic culture.
<i>Analisis faktor-faktor yang berpengaruh terhadap keterandalan dan ketepatanwaktuan pelaporan keuangan pada SKPD pemerintah daerah kota Kendari</i> (Analysis of factors affecting reliability and timeliness of financial reporting in local authority of Kendari)	Mustafa, et al. (2011)	Internal control and application of information technology affect reliability of financial statements, while capacity of personnel did not affect the reliability because these personnel still have low abilities and education regarding governmental accounting.
<i>Pengembangan sistem anggaran dan akuntansi Badan Layanan Umum Universitas Brawijaya: Sebuah studi interpretative</i> (Development of budgeting and accounting system of Brawijaya University as a state owned company: an interpretative study)	Amirya, et al. (2011)	This study indicated that adoption of budgeting and accounting systems is required to gain legitimacy.

<p><i>Perilaku opportunistik legislatif dalam penganggaran daerah: Bukti empiris atas aplikasi agency theory di sektor publik</i> (Opportunistic behaviour of the legislative in local government budgeting: Empirical evidence on application of agency theory in the public sector)</p>	<p>Abdullah, S. & Asmara, J.A. (2006)</p>	<p>This study indicated that legislative members behave opportunistically towards budgeting processes, which were affected by <i>Pendapatan Asli Daerah</i> (local government income); and <i>Anggaran Pendapatan Daerah</i> (local government budget) as a medium for corruption.</p>
<p>The influence of internal control systems on the reliability of local government financial statements (Case study at East Java Province)</p>	<p>Nugraha, D.S. (2010)</p>	<p>This study indicated the importance of the internal control system affecting reliability of financial statements. Especially two components of five components of internal control, i.e. the control environment, and information and communications affected the reliability of financial statements significantly.</p>
<p><i>Pengaruh tekanan eksternal, ketidakpastian lingkungan, dan komitmen manajemen terhadap penerapan transparansi pelaporan keuangan</i> (Influence of external pressures, uncertainty, and management commitment towards implementation of financial reporting)</p>	<p>Ridha, M.A. & Basuki H. (2011)</p>	<p>This study indicated that implementation of financial transparency was affected by external pressures, which were imposed through laws and regulation from the central government; and by management commitment.</p>
<p><i>Akuntabilitas dan transparansi dalam pertanggungjawaban pemerintah daerah untuk mewujudkan pemerintahan yang baik di daerah (Studi di Kabupaten Kebumen)</i> (Accountability and transparency as local government's responsibility to realise good corporate governance (Study in Kebumen district)</p>	<p>Rahmanurrasjid, A. (2008)</p>	<p>Involvement of the local parliament tends to be political and local society also has propensity to be apathetic toward accountability reporting</p>
<p><i>Studi evaluasi dampak pemekaran daerah 2001 - 2007</i> (Evaluation study of impact of local government enlargement)</p>	<p>Badan Perencanaan Pembangunan Nasional / Bappenas (2008)</p>	<p>This study suggested several points, i.e. low quality of local government officers; underemployed of the officers; and qualifications of the available officers do not fit with requirements.</p>

Governance and poverty reduction: Evidence from newly decentralised Indonesia	Sumarto, S., et al. (2004)	Bad governance affects poverty reduction significantly; local governments with better governance experience faster poverty reduction.
Do attitudes towards corruption differ across cultures? Experimental evidence from Australia, India, Indonesia, and Singapore	Cameron et al. (2005)	Results of this study in Indonesia indicated that recent democratisation and press freedom strengthen efforts against corruption.
Voice lessons: Local government organisations, social organisations, and the quality of local government	Alatas et al. (2002)	0This study indicated roles of social organisations to enhance performance of government institution in Indonesia.
Obstacles to public sector accounting reform in Indonesia	Harun (2007)	Improvement in accountability will thread overall income level of politicians and bureaucrats. In human resources aspects, this study indicated lack of accounting skills.

Appendix 7 List of Interviewees as Primary Sources

No.	District	Local Government Agency	Date of Interview	Number of Interviewee	Position of Interviewee	Code
1.	Bantul	Dinas Perhubungan	19 September 2013	2	Head of agency, and Finance department	HOA 1 SFO 1
2.	Bantul	Dinas Pendidikan Dasar	13 September 2013	1	Planning Department	SPO 1
3.	Bantul	Dinas Pendidikan Menengah dan Non-Formal	12 September 2013	3	Planning, and Finance Department	SPO 2 JPO 1 SFO 2
4.	Bantul	Dinas Kelautan dan Perikanan	11 September 2013	3	Planning, and Finance Department	SPO 3 JPO 2 SFO 3
5.	Bantul	Dinas Pekerjaan Umum	10 September 2013	3	Planning, Finance Department, and Secretary of agency	SPO 4 SFO 4 SOA 1
6.	Bantul	Inspektorat	01 October 2013	1	Head of agency	HOA 2

7.	Gunung Kidul	DPPKAD	23 August 2013	2	Head of the agency, and finance department	HOA 3 SFO 5
8.	Gunung Kidul	Dinas Peternakan	23 August 2013	3	Planning, and Finance Department	SPO 5 JPO 3 SFO 6
9.	Gunung Kidul	Dinas Pendidikan, Pemuda, dan Olahraga	20 August 2013	2	Secretary of the agency, and Finance department	SOA 2 SFO 7
10.	Gunung Kidul	Dinas Perhubungan, Komunikasi dan Informatika	21 August 2013	1	Planning department	SPO 6
11.	Gunung Kidul	Inspektorat	21 August 2013	2	Internal Auditor	SIA 1 SIA 2
12.	Gunung Kidul	RSUD Wonosari	21 August 2013	2	Planning, and Finance department	SPO 7 SFO 8
13.	Kulon Progo	RSUD Wates	19 September 2013	1	Secretary of agency	SOA 3
14.	Kulon Progo	Inspektorat	09 September 2013	1	Secretary of agency	SOA 4
15.	Kulon Progo	Dinas Kesehatan	03 September 2013	1	Head of agency	HOA 4
16.	Kulon Progo	Dinas Kebudayaan, Pariwisata, Pemuda dan Olahraga	06 September 2013	2	Head of agency and planning department	HOA 5 SPO 8
17.	Kulon Progo	Dinas Pendidikan	03 September 2013	2	Secretary of agency, and Finance department	SOA 5 SFO 9
18.	Kulon Progo	Dinas Kelautan, Peternakan, dan Perikanan	04 September 2013	1	Secretary of agency	SOA 6
19.	Kulon Progo	Dinas Pekerjaan Umum	04 September 2013	1	Head of the agency	HOA 6
20.	Sleman	Dinas SDAEM	18 September 2013	1	Planning department	SPO 9
21.	Sleman	Dinas Dikpora	23 September 2013	3	Finance, Planning, and Asset management	SFO 10 SFO 11 SPO 10
22.	Sleman	Inspektorat	03 October 2013	1	Head of agency	HOA 7
23.	Sleman	Dinas Perhubungan	03 October 2013	2	Secretary of agency, and Finance department	SOA 7 SFO 12
24.	Sleman	Dinas Pertanian	02 October 2013	1	Planning department	SPO 10
25.	City of Yogyakarta	Dinas Gedung, Bangunan, dan Aset Daerah	26 September 2013	3	Secretary of the agency, Planning, and Finance department	SOA 8 SPO 11 SFO 13
26.	City of	Dinas Lingkungan	26 September	1	Planning	SPO 12

27.	Yogyakarta City of Yogyakarta	Hidup Dinas Kesehatan	2013 25 September 2013	1	department Planning	SPO 13
28.	City of Yogyakarta	Dinas Perhubungan	25 September 2013	1	Planning department	SPO 14
29.	City of Yogyakarta	Dinas Pemukiman, Prasarana Wilayah	25 September 2013	2	Secretary of the agency, and Planning department	SOA 9 SPO 15
30.	Province of Yogyakarta	Inspektorat	29 August 2013	1	Planning department	SPO 16
31.	Province of Yogyakarta	DPPKAD	23 August 2013	4	Secretary of the agency, Finance, and Planning department	SOA 10 SFO 14 SPO 17 SPO 18
32.	Province of Yogyakarta	Dinas Pendidikan dan Pelatihan	15 August 2013	3	Secretary of the agency, Finance, and Planning department	SOA 11 SFO 15 SPO 19
33.	Province of Yogyakarta	Dinas PUP dan ESDM	15 August 2013	1	Secretary of the agency	SOA 12
34.	Province of Yogyakarta	Dinas Kelautan dan Perikanan	16 August 2013	1	Secretary of the agency	SOA 13
35.	Province of Yogyakarta	Badan Perpustakaan dan Arsip Daerah	14 August 2013	2	Head and secretary of the agency	HOA 8 SOA 14
36.	Province of Yogyakarta	Badan Penanggulangan Bencana Daerah	13 August 2013	2	Secretary of the agency, and planning department	SOA 15 SPO 20
37.	Province of Yogyakarta	RSUD Grahasia	19 August 2013	1	Secretary of the agency	SOA 16
TOTAL		37 Local Government Agencies			64 Local Government Officers	

Abbreviation:

JFO: Junior Finance Officer

JPO: Junior Planning Officer

HOA: Head of Local Government Agency

SFO: Senior Finance Officer

SIA: Senior Internal Auditor

SOA: Secretary of Local Government Agency

SPO: Senior Planning Officer

Appendix 8
List of Questions / Daftar Pertanyaan

1. Would you please tell me about capital expenditures in this province/city/district?
Tolong anda ceritakan mengenai beberapa belanja modal di provinsi/kodya/kabupaten?
2. Would you please tell me how does funding flow from central government to the specific project?
Bisakah anda jelaskan bagaimana mengenai pendanaan mulai dari pemerintah pusat sampai ke belanja modal tersebut?
3. Why does the province/city/district approve the particular expenditures and reject the other proposal of expenditures?
Mengapa provinsi/kodya/kabupaten menyetujui suatu belanja modal tertentu dan menolak pengajuan belanja modal yang lain?
4. Would you please tell me about your perception with regard financial systems and procedures?
Bagaimana menurut persepsi anda mengenai sistem keuangan dan prosedur pengendalian yang sudah ada saat ini?
5. What are difficulties in implementation of the capital expenditures in relation with other unit/other section/third parties, and with systems and procedures?
Apakah kesulitan yang dihadapi waktu implementasi belanja modal dalam kaitannya dengan unit lain/bagian lain/pihak ketiga, dan kepatuhan kepada sistem dan prosedur?
6. How do you deal with the difficulties?
Bagaimana cara mengatasi kesulitan-kesulitan tersebut?
7. What would you like to see done differently, if you have authorisation for it?
Apakah perbedaan yang ingin anda lakukan jika anda memiliki kewenangan untuk itu?

Appendix 9

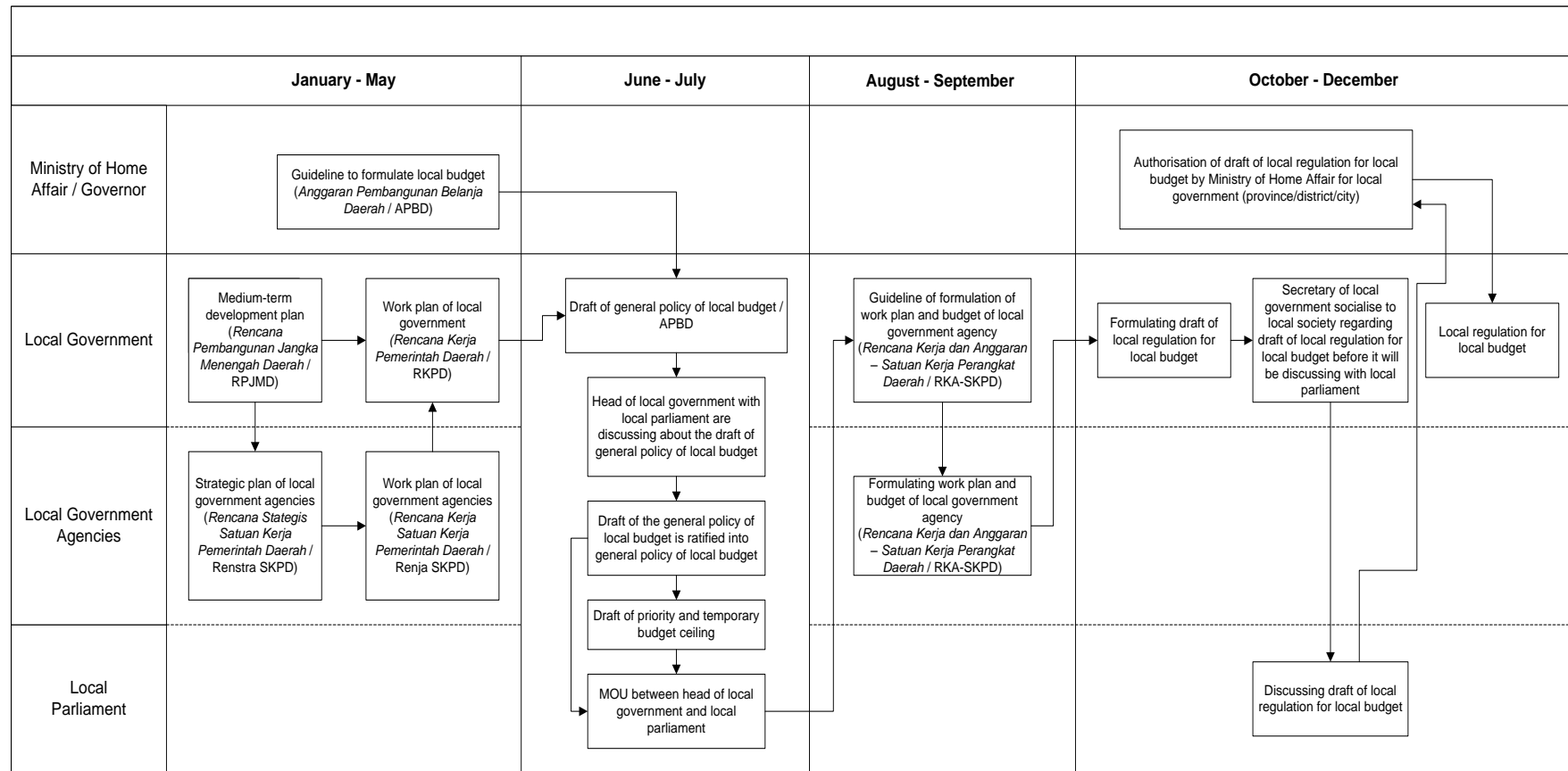
List of Secondary Sources

No.	Name of Interviewee	Position of the Interviewee	Date of Interview
1.	Emil Salim	An economic advisor to the late President Suharto, Vice-chairman of the National Planning Board, and held various cabinet-level positions for the improvement of state apparatus, communications, development supervision, the environment.	6 July 2009
2.	Erry Firmansyah	Former president of the Jakarta Stock Exchange (Indonesia Stock Exchange).	10 July 2009
3.	Erry Hardjapamekas	First appointed commissioner on the KPK (Komisi Pemberantasan Korupsi, Corruption Eradication Commission).	22 February 2012
4.	Erwin Ariadharma	A Senior Public Sector Management Specialist at the World Bank.	9 July 2009
5.	Hadi Soesastro	The executive director of the CSIS (Centre for Strategic and International Studies).	7 July 2009
6.	Juwono Sudarsono	The minister has been Minister for State, for the Environment, Minister for Education and Culture, the first civilian Minister of Defense in Indonesia's history, ambassador to the UK under then President (Megawati) Sukarnoputri and currently Minister of Defense since 2004.	7 July 2009
7.	Muhammad A.S. Hikam	A researcher at the Indonesian Institute of Sciences, a government-owned research institution, in Center for Economic and Development Studies (PEP-LIPI) from 1983 until 2001. Appointed as a cabinet minister in 1999.	14 July 2009
8.	Rizal Ramli	Headed the nation's State Logistics Agency and most notably was Coordinating Minister for Economic Affairs under the administration of President Abdurrahman Wahid, and also Minister of Finance.	15 July 2009
9.	Robert Pakpahan	The Director of Business Processes Transformation at the DG (Directorate General) Tax in the Ministry of Finance in Indonesia, which is basically in charge of improving or developing current processes, mostly administrative aspect of these organizations.	16 July 2009

10.	Sarwono Kusumaatmadja	Had a longstanding involvement with Indonesian politics, most notably as secretary-general of the Golkar Party, state minister for Administrative Reform, and minister for the Environment under President Suharto, minister of Maritime Affairs.	9 July 2009
11.	Siti Nurbaya	Had an important role in implementing Indonesia's decentralization policy as the secretary general of the Ministry of Home Affairs from February 2001 to May 2005.	7 June 2010
12.	Sri Mulyani Indrawati	The Minister of Finance (former).	14 July 2009

Appendix 10

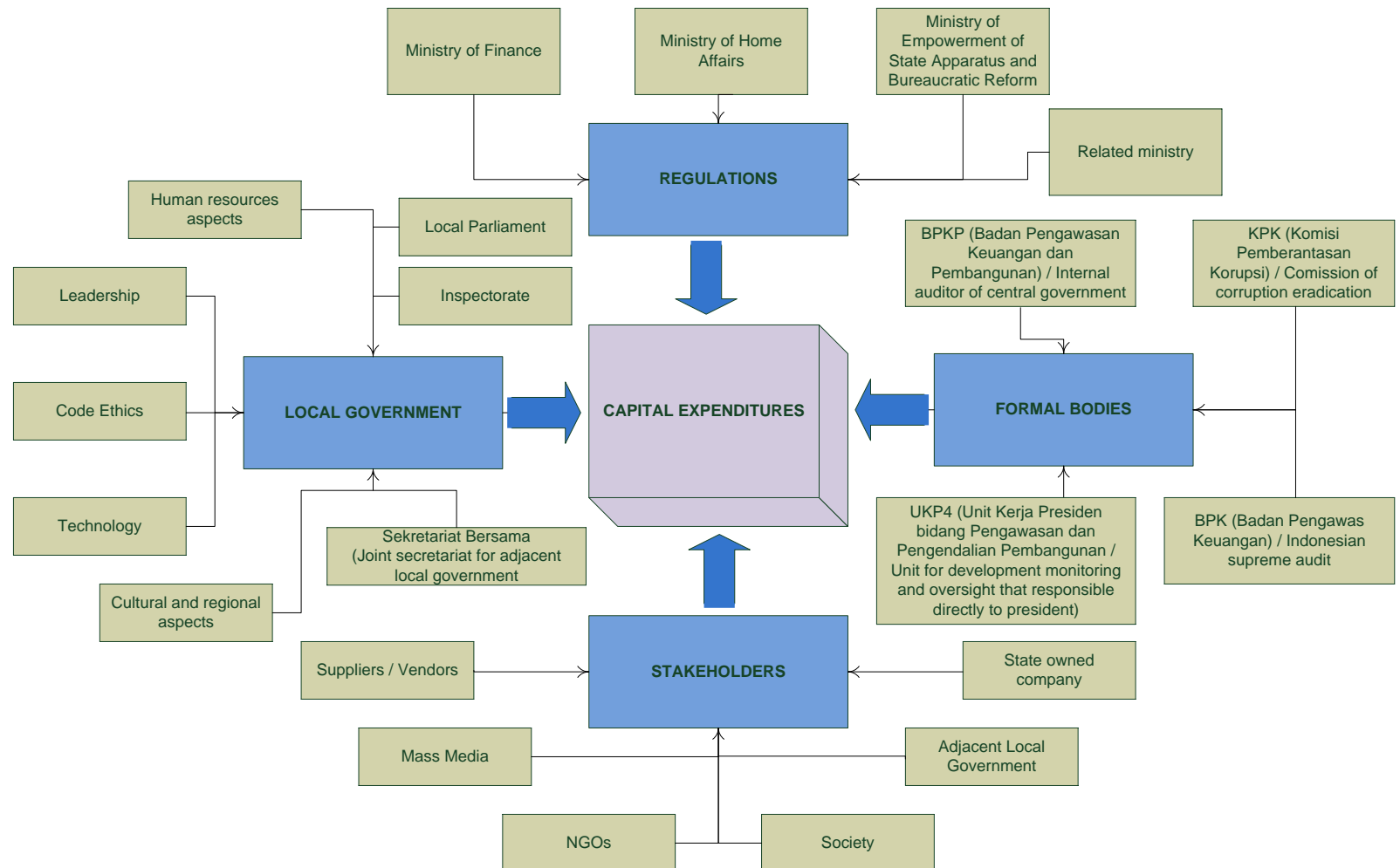
Flowchart of Planning Process of Local Government Agencies along with the Timeline



Source: Rancangan Pedoman Umum Perencanaan Pengadaan Barang/Jasa Pemerintah di Lingkungan Kementerian/Lembaga/Satuan Kerja Perangkat Daerah/Institusi Lainnya, LKPP (Lembaga Kebijakan Pengadaan Barang/Jasa Pemerintah, Appendix 2.3)

Appendix 11

Research Finding



Appendix 12

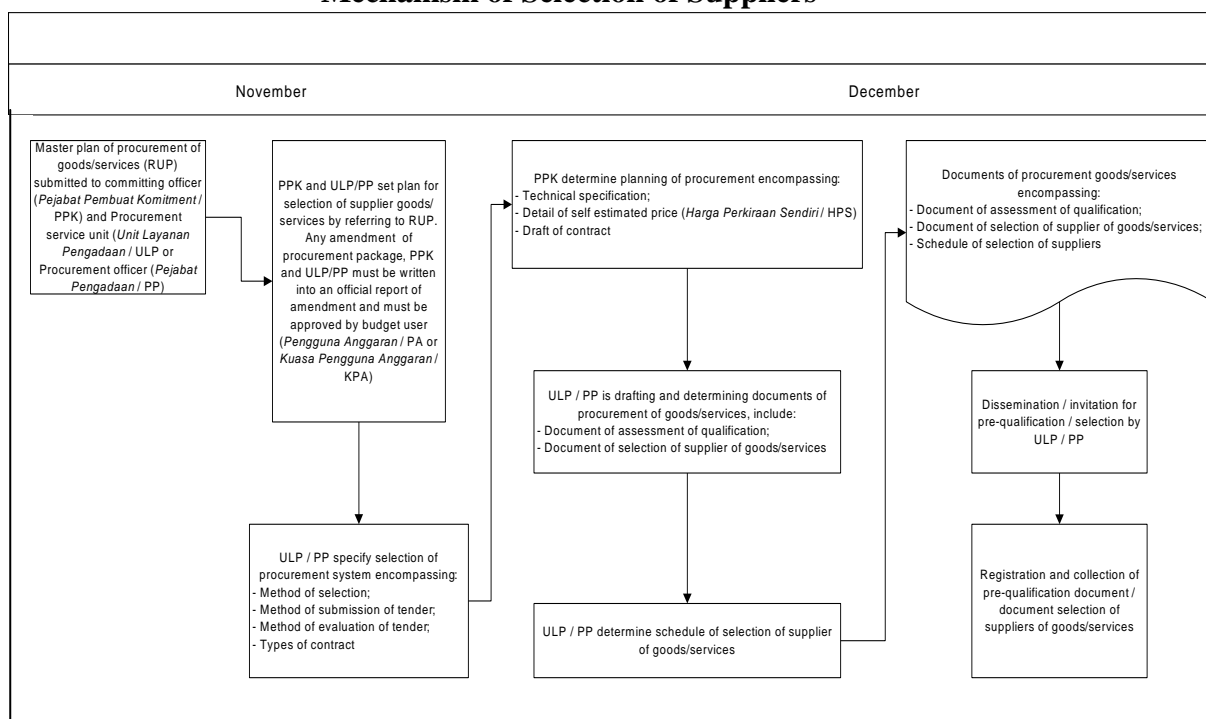
Evolving Regulations Concerning Capital Expenditure

Regulations in Pre-reform Era			Regulations in Post-reform Era			
Government Regulation 36 / 1972	Presidential Decree 16 / 1994	Presidential Decree 24 / 1995	Presidential Decree 18 / 2000	Presidential Decree 80 / 2003	Presidential Decree 54 / 2010	Presidential Decree 70 / 2012
<p>This regulation distinguished two types of local budget, i.e. Routine budget and development budget. The latter budget was specified based on field, sector/sub-sector, programme, and project/sub-project.</p> <p>Regarding local government expenditures, the head of local government has authority to spend funds as long as it was outlined in the local budget that has been approved by the local parliament.</p> <p>All spending must be accompanied by SKO (<i>Surat Keputusan Otorisasi</i> / Official letter of authorisation) issued by the head of local government.</p> <p>Any invoice from a supplier must be accompanied with</p>	<p>This presidential decree had indicated four ways that goods or services may be procured.</p> <ul style="list-style-type: none"> - Public Tender, - Limited Tender, - Direct selection, - Direct Appointment. <p>Public tender was open to all qualified bidders.</p> <p>Limited tender relates to procurement in which a minimum of five potentials suppliers who are listed in government database to participate.</p> <p>Direct selection was procurement without tender. It involves comparing technical specifications and prices from at least three potential suppliers.</p> <p>Direct appointment was procurement without tender or selection, because it was directed</p>	<p>This presidential decree was intended to revise several articles of Presidential Decree 16/1994.</p> <p>Direct appointment was directed to small enterprises. Hence, it did not need public or limited tender or direct selection.</p> <p>Meanwhile, the direct selection can be performed for projects between IDR15 million to IDR50 million.</p> <p>At the province level, direct selection of supplier can be undertaken for projects between IDR50 million to IDR1 billion.</p> <p>Projects between IDR1 billion to IDR5 billion must be approved by the Ministry of Internal Affairs. Above IDR5 billion must be approved by Coordinator Ministries</p>	<p>This presidential decree has emphasised roles of heads of local government agencies as both budget user and procurement committee.</p> <p>Officers authorised to determine suppliers of goods or services were:</p> <ul style="list-style-type: none"> - Head of local government agency responsible for direct selection or direct appointment for procurement up to IDR50 billion, - Head of local government for procurement above IDR50 billion, or Governor if the procurement was funded by the province. 	<p>In this decree, the procurement officers started to have roles to handle procurement up to IDR50 million.</p> <p>Meanwhile, procurement above IDR50 million will be handled by the procurement committee.</p> <p>Selection of suppliers through four method, i.e. public tender; limited tender for complex work; direct selection from at least three supplier for procurement up to IDR100 million; and direct appointment of a supplier in specific circumstances or maximum worth IDR50 million.</p> <p>Cash paid in advance for small enterprise supplier was set up to</p>	<p>This presidential decree initiated the establishment of LKPP (<i>Lembaga Kebijakan Pengadaan Barang/Jasa Pemerintah</i> / Agency formulating policies of government procurement), and determined each actor in procurement, along with their roles.</p> <p>Procurement was undertaken in several ways:</p> <ul style="list-style-type: none"> - Public tender for all qualified suppliers to participate; - Limited tender for complex works; - Simple tender for procurement worth up to <u>IDR200</u> million; - Direct selection for construction work that has a maximum value of IDR200 million; - Direct appointment 	<p>This presidential decree revised the previous decree.</p> <p>The involvement of the ULP is revised from IDR100 million to IRDR200 million up to IDR100 billion for construction work; and consultancy services limits remain the same IDR50 million up to IDR10 billion.</p> <p>Any work worth below IDR200 million or consultancy services below IDR50 million can be undertaken by a procurement officer</p> <p>Complex work is defined as work worth at least IDR100 billion.</p>

supporting documents that was stipulated by the head of local government.	for small enterprises.	of Economic, Finance, and development.		30% of value of contract; meanwhile for other enterprises was up to 20% of the value of the contract.	in which one supplier is appointed;
The amount of cash in advance that will be paid to a supplier was determined by the head of local government and local parliament.	Implementation of procurement was regulated as follows:	In the municipal level (city or district), direct selection can be performed for projects between IDR50 million and IDR500 million.	Evaluation of bidder of tender will be undertaken through three method, i.e.	A 'small enterprise' was defined as a company that has maximum net assets of IDR200 million and maximum net sales of IDR1 billion per annum. In addition, the company is not a subsidiary of a medium or large company.	- Direct appointment/procurement.
Any project with value exceeding that which had been determined, must be undertaken through general procurement or limited procurement.	- Up to IDR5 million limit for the direct appointment of small enterprises,	Projects between IDR500 million to IDR1 billion can be performed if acquired approval from the governor. Projects from IDR1 billion to IDR5 billion must get approval from the Ministry of Internal Affairs. Finally, projects above IDR5 billion must have approval from Coordinator Ministries of Economic, Finance, and Development.	- Single-elimination system - Value system - Live cycle cost.	A foreign company was allowed to participate in procurement with requirements as follows:	This decree became the foundation for the establishment the ULP (<i>Unit Layanan Pengadaan</i> / Procurement service unit). Any procurement or construction work above IDR100 million up to IDR100 billion, and consultancy services worth above IDR50 million up to IDR10 billion must be procured by the ULP.
Cash paid in advance may not exceed 20% of the value of the total project after the supplier submitted a bank guarantee.	- From IDR5 million to IDR15 million for direct appointment referring to list of head of local government,		Cash in advance can be paid based on the contract.		
Head of local government undertook public or limited tenders, and appoints the most favourable bidder.	- From IDR15 million to IDR50 million was direct selection from at least three potential suppliers,				
Local government officers are not allowed to participate in any project from local government directly or indirectly.	- Above IDR50 million was undertaken through public or limited tender.			- Construction with value above IDR50 billion, - Other goods/services for value above IDR10 billion, - Consultancy services worth IDR5 billion	Meanwhile, procurement for goods/services worth below IDR100 million, or IDR50 million for consultancy services can be undertaken by either the ULP or a procurement officer. Procurement below IDR200 million can be undertaken by simple tender or direct selection.

Assumption: at that time US\$1 was equal approximately IDR2,000; currently USD\$1 is equal IDR14,000

Appendix 13 Mechanism of Selection of Suppliers



Source: Rancangan Pedoman Umum Perencanaan Pengadaan Barang/Jasa Pemerintah di Lingkungan Kementerian/Lembaga/Satuan Kerja Perangkat Daerah/Institusi Lainnya, LKPP (Lembaga Kebijakan Pengadaan Barang/Jasa Pemerintah, P.52

Appendix 14 Leading sectors in Each Region of D.I. Yogyakarta Province

Main Industry	Region				
	Kulon Progo	Gunungkidul	Bantul	Sleman	City of Yogyakarta
Agriculture	50.24%	54.41%	16.98%	18.86%	0.25%
Manufacturing Industry	11.61%	8.56%	21.78%	11.83%	9.78%
Wholesale, Retail Trade, and Restaurant	17.80%	15.70%	26.62%	28.54%	47.57%
Services	12.17%	12.31%	20.95%	25.66%	26.28%
Others	8.18%	9.02%	13.67%	15.12%	16.12%

Source: Badan Pusat Statistik D.I.Yogyakarta (Central Agency on Statistics of the Special Region of Yogyakarta), 2014, p.95

Appendix 15

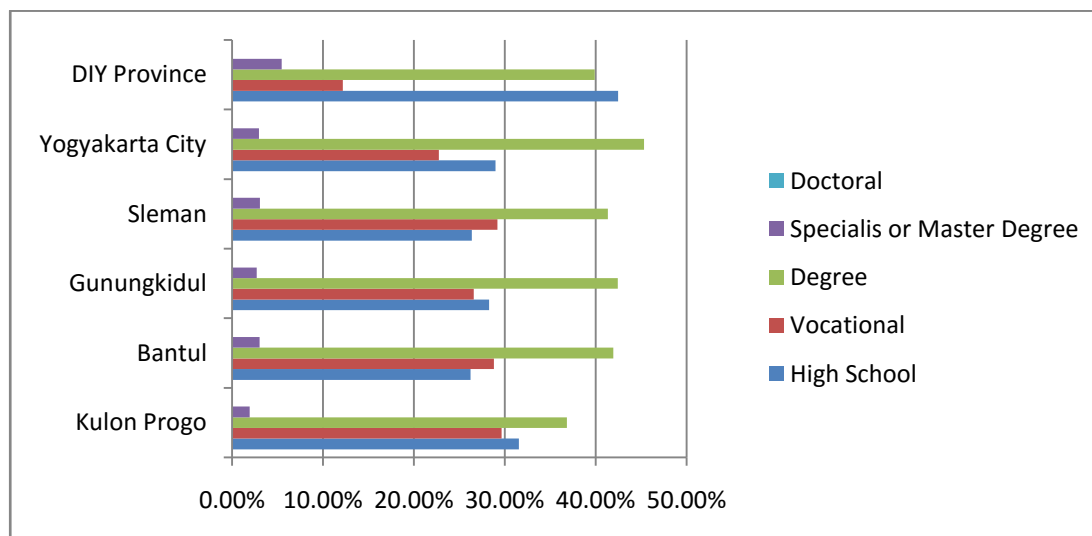
Distribution of Civil Servants Based on Their Levels of Education

Level of Education	Region					
	Kulon Progo	Bantul	Gunungkidul	Sleman	Yogyakarta City	DIY Province
High school	31.56%	26.22%	28.29%	26.39%	28.98%	42.46%
Vocational	29.65%	28.80%	26.57%	29.19%	22.75%	12.19%
Degree	36.83%	41.93%	42.41%	41.34%	45.32%	39.88%
Specialist or Master Degree	1.95%	3.05%	2.72%	3.06%	2.95%	5.45%
Doctoral	0.01%	0.00%	0.01%	0.02%	0.00%	0.03%

Source: Badan Pusat Statistik D.I.Yogyakarta (Central Agency on Statistics of the Special Region of Yogyakarta), 2014, p.77

Appendix 16

Distribution of Civil Servants Based on Their Levels Education



Source: Badan Pusat Statistik D.I.Yogyakarta (Central Agency on Statistics of the Special Region of Yogyakarta), 2014, p.77

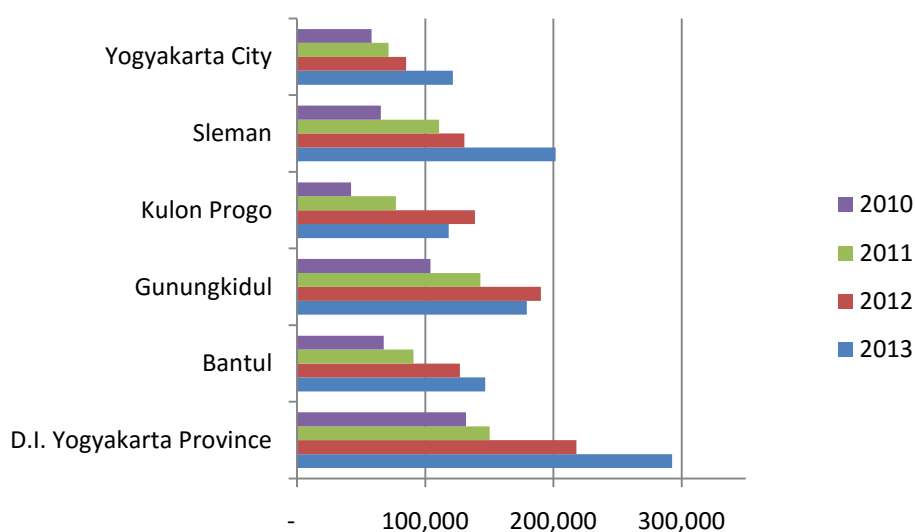
Appendix 17
Capital Expenditure in Regions of the Province of D.I. Yogyakarta

	Province of D.I. Yogyakarta	Region of Bantul	Region of Gunungkidul	Region of Kulon Progo	Region of Sleman	City of Yogyakarta
2013	292,505	146,797	179,342	118,397	201,672	121,557
2012	217,959	127,094	190,308	138,686	130,674	85,153
2011	150,174	90,932	143,141	77,093	110,782	71,352
2010	131,691	67,552	104,126	42,170	65,333	58,270

(in IDR millions, exchange rate \$1=IDR14,000)

Source: <http://www.kemenkeu.go.id/Page/data-keuangan-daerah>

Appendix 18
Capital Expenditure in Regions of the Province of D.I. Yogyakarta



(in IDR millions, exchange rate \$1=IDR14,000)

Source: <http://www.kemenkeu.go.id/Page/data-keuangan-daerah>